No. 76-226

In the Supreme Court of the United States

OCTOBER TERM, 1975

In Re CRATEO, INC.,

Bankrupt,

CRATEO, INC.,

Petitioner,

v.

INTERMARK, INC., et al.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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TOPICAL INDEX

TOPICAL INDEX (Continued)

CITATIONS

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The Petitioner, Crateo, Inc., respectfully prays that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit.

OPINION BELOW

The opinion of the Court of Appeals for the Ninth District, not yet reported, appears in the Appendix. No opinion was rendered by the District Court.

JURISDICTION

The opinion and judgment of the United States Supreme Court of Appeals for the Ninth Circuit was entered on May 27, 1976 affirming a judgment of the United States District Court for the Southern District of California dated August 7, 1973 (____F.3d____). The United States Court of Appeals (Ninth Circuit) denied a timely petition for rehearing on June 28, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

QUESTIONS PRESENTED

1. Does a corporation commit the fifth act of bankruptcy by seeking State Court supervision over its voluntary dissolution where no appointment is made by the court of an indifferent person as a receiver?

2. Does a construction of Bankruptcy Section 3a(5) permitting conversion of the directors of a corporation into trustees for creditors without the consent of the directors, the consent of the shareholders, or the consent of the creditors:

a. Impose fiduciary duties to creditors upon directors without their consent and without "due process"?

b. Force directors into the servitude of creditors?

c. Deprive shareholders the control of the corporation without "due process"?

d. Deny creditors the right to have or select a disinterested receiver or trustee?

e. Place directors in jeopardy of both California law and Federal decisions which preclude "interested parties" such as directors, from acting as trustees?

3. What is the effect of presenting as a bona fide claim a judgment which represents 40% of the total claims and which is subject to attack for fraud?

4. Should a litigant be required to go to another forum to attack that fraud when concealment of the fraud took place in the court below and after a receiver has been appointed over the litigant's assets?

5. Is the statutory right to a jury trial denied where a Master (who is a Judge in the same district) is appointed who finds upon the ultimate question to be presented to the jury?

6. Is an installment judgment, or installment note, a "mature" debt in the bankruptcy sense as to installments not yet due?

STATUTORY PROVISION INVOLVED

Bankruptcy Act Section Three, 11 USC Section 21:

"a. Acts of bankruptcy by a person shall consist of his having. . . .

(5) while insolvent or unable to pay his debts as they mature, procured, permitted, or suffered voluntarily or involuntarily the appointment of a receiver to take charge of his property."

STATEMENT OF THE CASE

This petition raises questions concerning the interpretation of Section 3a(5) of the Bankruptcy Act and the use of a special master whose findings upon the ultimate issue in the case is given to the jury to take with them to the jury room.

Crateo, Inc. was a corporation which elected to voluntarily dissolve. Under California law, it was permitted to seek California Court supervision over the winding up process, which it did.

No receiver or trustee was appointed by the Court.

The California court, acting under statutory authority, issued a restraining order against creditors from litigating elsewhere, and required creditors to file their claims and proceed in that Court, thereby marshalling all litigation in that one court.

A Creditors' Petition in Involuntary Bankruptcy against Crateo was thereafter filed alleging that (1) Crateo was "unable to pay its debts as they mature" and (2) that by electing to dissolve and filing a Petition for Voluntary Dissolution it had the "legal effect to cause the Board of Directors to become 'Trustees' within the meaning of Section 3a(5) of the Bankruptcy Act." Crateo denied the petition.

At no time was any claim made by the creditors that Crateo's liabilities exceeded its assets, (insolvency). The only claim was that it was unable to pay its debts as they matured, (illiquidity).

After filing for dissolution Crateo continued to hold title to its assets, the directors got no title; the directors of Crateo continued to act as a Board of Directors and to run the business of Crateo; they filed no bond; they took no oath of loyalty to creditors; they continued to represent the shareholders; they obtained an injunction against the creditors; they

contested the involuntary petition in bankruptcy filed by the creditors; they filed four successive appeals and are before this Court.

In other words, the directors were, and continued to be, representatives of the shareholders, and were adverse, and continued to be totally adverse, to creditors. (The Ninth Circuit below on this point determined that even though there was no appointment by the State Court of a receiver or trustee to take charge of its property as required under Section 3a(5) of the Act, the mere seeking and receiving of the restraining order marshalling litigation before one Court under the California Statute, assuming inability to pay debts as they matured, amounted to the fifth act of bankruptcy.)

Crateo requested a jury trial. The District Court, however, referred the case to a judge who was a referee in bankruptcy in the same court system, and appointed him as a Master.

The Master made findings upon the ultimate question posed to the jury - whether Crateo, Inc. had debts which it was unable to pay as they matured. Those findings were not only read to the jury, but delivered in written form into the jury room without any request therefor by the jury. Cross examination of the Master was denied.

The Master's report made a formal finding that Crateo had $750,621.56 in 13 "debts" within the meaning of 3a(5) of the Bankruptcy Act. (*i.e.* that they were "mature.")

The so-called "mature" debts of Crateo discussed by the Ninth Circuit were:

(a)	Intermark Investing, Inc.	$229,848	30.6%
(b)	Southern National Bank of Houston	293,647	40.4%
(c)	Olympia Business Service	90,000	12.0%

The Intermark debt, constituting 30.6% of the entire sum found mature, arose from a stipulated "mixed" judgment for $229,848 calling for both "payment in installments" of only $5,000 per month and "performance." The judgment was secured by two parcels of property. Crateo, in addition, deeded the two parcels to Intermark.

Only one installment payment of $5,000 was owing to Intermark at the time of the involuntary bankruptcy petition. Since Intermark was secured by judgment lien and had deeds to the properties, it could have sold them and prepaid the installments of the judgment.

The Olympia Business Service debt (constituting 12% of the debt) was an installment note, the principal of which could be accelerated only upon 30 days' notice. The Master took note of the "notice" requirement, but failed to find that "notice" had been given. There is no testimony that such notice was given. Crateo contended that, absent notice, the principal was not mature, but that only two delinquent installments were mature.

The Master and the Ninth Circuit, despite the fact that unpaid installments were not due for either the Intermark installment judgment or the Olympia installment note, found the entire principal to be "mature." The Ninth Circuit used the word "fixed."

There was undisputed evidence upon which the jury could have found that Crateo, Inc. could pay its debts as they matured: Crateo, Inc. paid its non-disputed debts as they matured. (R.T. 282, line 3). It had over 800 vendor creditors who were constantly being paid. (R.T. 292, lines 1-3.) Crateo made deposits of $811,617.69 to its bank account at the end of August, September, October and November (R.T. 292-294). The balance sheet showed assets of $4,580,643 and total liabilities of $2,238,174. (R.T. 402, line 11). Finally, the creditors did not claim or allege insolvency.

POST-JUDGMENT

While the matter was pending on appeal, it was discovered that a judgment presented in evidence to show that Crateo, Inc. was unable to pay its debts as they matured, was procured by extrinsic fraud and concealment of an adjudication of forgery.

Southern National Bank of Houston had secured a judgment, not yet final, for not purchasing, as agreed, a promissory note purportedly issued to the bank by Toni Clark and others. The case is reported at 317 Fed.Supp. 1173 (July 29, 1970, Texas District Court). The note was never produced at the trial.

While that case was pending on appeal, and while the judgment thereon was being presented in the bankruptcy case below, the same plaintiff, Southern National Bank of Houston, in a Federal District Court in Nevada, suffered an adjudication that the purported signature of the maker, Toni Clark, was a forgery. This adjudication was concealed from the District Court in Texas and from the 5th Circuit, whose divided decision affirming, is reported at 458 Fed.2d 688, April 19, 1972, and from the Master and from the District Court below.

The claim for $293,647, founded on a forgery, constituted 40.4% of the claimed "mature" debt.

Appropriate and timely post-judgment motions were made and appropriate relief was sought. But all of those motions were met with the contention that the alleged bankrupt could not meet the issue in the Court below, where the proceedings were still alive, but must return first to Texas, where they were not, and seek to reopen there.

REASONS FOR GRANTING THE WRIT

I.

The Ninth Circuit Conflicts Squarely With The Second Circuit On Whether There Must Be (1) An Appointment; (2) By A Court; (3) Of An "Indifferent Person" In Order To Constitute An Act Of Bankruptcy Under Section 3a(5)

The Ninth Circuit, in its opinion below, stated relative to the Fifth Act of Bankruptcy:

> "There was no need for the Board of Directors to be formally appointed trustees or to formally possess legal title to the corporation's assets."

That opinion conflicts squarely with the opinion of the Second Circuit in *Blair & Co., Inc. v. Foley* 471 F.2d 178 (1972) which holds there must be an *"appointment" "by a Court"* of an *"indifferent person."*

In the Second Circuit case of *Blair & Co., Inc. v. Foley,* 471 F.2d 178 (1972) the court ruled that a private appointment of a liquidating agent by the stock exchange, while *Blair* was insolvent, did not result in commitment of the fifth act of bankruptcy. There had to be an appointment by a court of a receiver or trustee of an indifferent person between the parties to a cause.

The Supreme Court granted certiorari in 411 U.S. 930, 93 S.Ct. 1901, 36 L.Ed. 389 (73). It heard oral argument on November 12, 1973 but then dismissed the petition for mootness when the case no longer had a live controversy because the parties had accepted a Chapter XI plan. 414 U.S. 997.

The Second Circuit in *Blair* stated that what *Foley* presented as a policy argument was, in reality, a contention that

Congress made a wrong turn when it required creditors to establish an act of bankruptcy and did not permit the setting of the procedures of the Bankruptcy Act in motion by a showing of insolvency alone. *Blair, supra,* p. 184. Here the Ninth Circuit has gone the whole way by holding that a corporation which has neither assigned its assets to anyone nor had a trustee or receiver appointed has nevertheless committed the fifth act of bankruptcy which requires a receiver or trustee to be appointed to take charge of his property.

In the case below the corporation elected to voluntarily dissolve. California law provides that upon such procedure, the corporation's board of directors continues to act as a board, but is limited to such matters as winding up and dissolution. California Corporations Code 4800; 4801. California law provides that the Superior Court may supervise the winding up. Acting under that statutory authority, the Superior Court issued restraining orders requiring the creditors of Crateo, Inc. to litigate all their claims against Crateo, Inc. before the one Court.

The creditors alleging the fifth act of bankruptcy was committed, rested their contention upon the claim that the mere act of electing to dissolve plus the issuance of a restraining order by the Superior Court which marshalled the litigation into one court satisfied the requirement of Section 3a(5) of the Act that there be the appointment of a receiver or trustee to take charge of its property.

It is now appropriate to outline the history of the Act:

In the 1898 Bankruptcy Act, as amended in 1903, the language provided that an act of bankruptcy was committed where "because of insolvency, a receiver or trustee has been put in charge of this property under the laws of the state." Under that language the trustee did not have to be put in charge by an order of a court, but the language embraced all the other

methods by which the property of an insolvent is committed to a trustee for creditors under the laws of a state. *In re Hercules Atkins,* (D.C. Pa.) 13 Am. B.R. 369, 133 F. 813 (1904).

In the 1926 version of the Act, Congress provided alternative grounds for the act of bankruptcy. Thus, in 1926 the language of Section 3a(5) of the Bankruptcy Act read:

> ". . . while insolvent, a receiver or trustee has been appointed or put in charge of his property."

Under the 1926 Act either the appointment of a trustee or merely "the putting of a Trustee in charge" of his property sufficed for the Act of Bankruptcy.

In the 1938 version Congress completely eliminated that very language of "put in charge" which had been the subject of *In re Hercules Atkins, supra,* which the Court had construed as covering a trustee who had not been appointed by a court. In the 1938 version Congress firmly required that:

> ". . . while insolvent, or unable to pay his debts as they mature, procured, permitted or suffered voluntarily or involuntarily the appointment of a receiver or trustee to take charge of his property."

Under the 1938 Act, which governs this case, therefore, it is no longer sufficient to "put someone in charge." A trustee must have been "appointed to take charge of his property."

When Congress made its 1938 version of the Act, it had before it the earlier language and the interpretation of that language in such cases as *In re Hercules Atkins, supra,* the very sort of interpretation contended for by the Ninth Circuit below. This was the language which Congress eliminated in 1938 when it deleted the provision that an Act of Bankruptcy might be

committed where a receiver or trustee is "put in charge of his assets." This left as the exclusive method the "appointment" of a receiver or trustee. The language in the subjunctive permitting as an additional ground the putting of a receiver or trustee in charge, having been eliminated, the Congress was expressly nullifying the interpretation of that language as set forth in *In re Hercules Atkins, supra.*

2A Sutherland, on Statutory Construction, Section 45.12, page 37, states that judicial interpretation of statutes is conditioned by various conditional presumptions which the courts indulge in. This "legislative language will be interpreted on the assumption that the legislature was aware of existing statutes, the rules of statutory construction and judicial decision that if a change occurs in legislative language the change was intended in legislative result."

In support of the rule that "if a change occurs in legislative language a change was intended," Sutherland cites, among other cases, *People v. Valentine,* 28 Cal.2d 121, 169 Pac.2d 1 (1946).

In *People v. Valentine, supra,* the court held that where a statute with reference to one subject contains a given provision, the omission of such provision in a similar statute concerning a related subject is sufficient to show that a different intent existed. It is presumed that the legislature by deleting an express provision of a statute intended a substantial change in the law.

The inquiry then becomes: What did Congress mean when it required that the receiver or trustee be "appointed to take charge of his property?"

The term "appointment" means the designation of a person, by the person having authority thereof, to discharge the duties of some office or trust. *Orphant v. St. Louis State Hospital Div. of Mental Diseases* (Mo.) 441, SW2d, 355, at 360.

In *Blair, supra,* at 181, the Second Circuit stated:

> "It is undisputed that two of the conditions of Section 3a(5) were here fulfilled. *Blair* was insolvent or unable to pay its debts as they matured, and it permitted the appointment of Scorese to 'take charge' of its property in the ordinary meaning of that term. But that is not enough unless *Blair* permitted Scorese to be appointed as a 'receiver or trustee.'"
>
> "The liquidator did not meet what is usually regarded as essential to the status of a receiver, namely: Appointment by a Court."
>
> "A receiver is an indifferent person between the parties to a cause, or appointed by the court pendente lite when it does not seem reasonable to the court that either party should hold it. He is not the agent or the representative of either party to the action, but is uniformly regarded as an officer of the court."

Thus, the Second Circuit, in *Blair, supra,* holds that there must be an *"appointment" "by a court"* of an *"indifferent person."* It is obvious that the board of directors of Crateo, Inc. was not appointed by a court; it was not an indifferent entity. The board was the representative of the stockholders. It was not a neutral person. To the contrary, it vigorously opposed the creditors. Under the specific rule of *Blair, supra,* the petition of Crateo in dissolution could not constitute the appointment of a receiver to take charge of the property.

The Second Circuit in *Blair* further required that trustees have title to the property. Under the express ruling of *Blair, supra,*

the board of directors "lacked one element essential to the normal concept of trusteeship, namely: Legal title to the property." In this respect, the *Blair* case differs essentially from the Crateo case below and *In re Bonnie Classics, Inc.*, 116 F.Supp. 646 (S.D.N.Y. 1953) on which the Master in the court below mistakenly relied. As title to *Blair's* property did not pass to the liquidator he could not be a trustee. Similarly, under applicable California corporate law, title to a corporation's property remained with the corporation and it never became vested in the Crateo directors.

Since the essential element of passage of title is lacking the directors of Crateo never became "trustees." The Ninth Circuit, accordingly, also contradicts the Second Circuit on the issue of the necessity of "title."

Summing up:

The *Blair* case of the Second Circuit, rather than the *Crateo* case of the Ninth Circuit, appears more clearly to coincide with the intent of Congress and the wording of the 3a(5) Act in requiring:

1. an appointment;
2. by a court;
3. of an indifferent person.

II.

The Ninth Circuit Decision Which Permits Conversion Of Directors Into Trustees Or Receivers Without The Consent Of The Directors, The Shareholders And The Creditors, Creates Serious Constitutional Problems

The Ninth Circuit held that the effect of Crateo's actions (filing for dissolution) was to require its board of directors to act as trustees for creditors.

That opinion, however, ignores the facts that (1) the directors did not consent to act as trustees, (2) the shareholders did not

consent to have the directors act adversely to the corporation; (3) the creditors did not consent to have the directors act for them; (4) the directors took no oath of loyalty to creditors; in fact, they continued to act adversely to the creditors; and (5) the directors contested the involuntary petition filed by the creditors, filed four appeals, and now are petitioning this Honorable Court.

California Corporations Code Section 4800 states:

> "When voluntary proceedings for winding up or dissolution of a corporation have been commenced, *the board of directors shall continue to act as a board. . . .*"

California Corporations Code Section 4801 states:

> "The powers and duties of the directors after commencement of such proceedings include, but are not limited to, the following *acts in the name and on behalf of the corporation:*
>
> "(b) *To continue the conduct of the business* insofar as necessary for the disposal of winding up thereof."

The Ninth Circuit's opinion creates these profound constitutional problems:

1. Fiduciary duties to creditors would be imposed upon directors without "due process."

Under the Ninth Circuit's thesis Bankruptcy Section 3a(5) alters the California Corporations Code relative to directors. The directors would owe a "fiduciary duty" to the creditors forthwith upon filing the voluntary dissolution proceedings. Yet, clearly, the directors accepted no such fiduciary duty to creditors. To impose a "fiduciary duty to creditors" upon the directors contrary to the directors' wishes and without notice and hearing, violates the "due process" required by the 14th Amendment to the Constitution.

2. Directors would be forced into the involuntary servitude of the creditors.

The directors were elected by the stockholders and assumed office to serve the stockholders. They owe allegiance to the stockholders. To require those directors, without their consent, to serve the creditors, whose interests are adverse to the stockholders, imposes an involuntary servitude upon the directors in violation of the 13th Amendment of the Federal Constitution.

3. Shareholders would be deprived of control of the corporation without "due process."

To convert directors of corporations into trustees for creditors on filing of dissolution proceedings would deprive the shareholders of their control over the corporation and to that extent deny them of their property rights without "due process of law" and violate the 14th Amendment to the U. S. Constitution.

4. Creditors are denied their statutory right to select a trustee as provided by Section 44 of the Bankruptcy Act (11 U.S.C. Sec. 72).

Under Section 44 of the Act the creditors (exclusive of a corporation stockholders, officers or directors) have the right to make the appointment. It flies in the face of Section 44 to permit the corporation itself to make its directors the trustees by filing for dissolution. The creditors are denied their right to select a disinterested trustee.

5. Directors would be placed in civil jeopardy for violation of state law.

California Civil Code Section 566 precludes parties or persons interested in the action from being appointed receiver.

III.

The Ninth Circuit Conflicts With Both California Statute And The Eighth Circuit On The Need For A Disinterested Trustee.

After filing for dissolution the directors of Crateo continued to act as a board of directors and to run the business of Crateo; they filed no bond; they took no oath of loyalty to creditors; they continued to represent the shareholders; they obtained an injunction against the creditors; they contested the involuntary petition in bankruptcy filed by the creditors; they filed successive appeals; and they are before this Honorable Court.

The directors were, and continued to be, representatives of the shareholders; and were adverse, and continued to be totally adverse, and hostile to creditors.

The Ninth Circuit, however, held that after dissolution commenced:

> "The net effect of this change means that Crateo's actions in the State Court resulted in the 'appointment of a receiver or trustee' within the meaning of 11 USC Sec. 21(a)(5)."

The Ninth Circuit did not discuss the California Section which precludes "interested parties" from being appointed receiver or trustee, or the Eighth Circuit's holding in *R. J. Reynolds Tobacco Co., et al v. A. B. Jones Co., Inc. et al*, 54 F.2d 329 (1931) that a receiver should be without interest.

California Civil Code Section 566 recites:

> "no party . . . or person interested in the action . . . can be appointed receiver. . . ."

The Eighth Circuit in *R. J. Reynolds, supra,* recited at page 334:

> "A receiver in bankruptcy . . . should be entirely without interest or embarrassing

> connection so far as any party to the bankruptcy is concerned."

Then, speaking of the president and director of the bankrupt who had been appointed, the Eighth Circuit stated:

> "He had embarrassing connections, and would necessarily be regarded by the creditors as a hostile receiver."

We thus have this conflict that should be resolved. The Ninth Circuit in the Crateo case holds that interested parties (*i.e.* directors) notwithstanding their hostility to creditors, became converted into receivers or trustees for creditors; while the California State Law precludes interested parties from being appointed receiver; and, the Eighth Circuit holds receivers should be without interest.

IV.

The Opinion Of The Ninth Circuit Permitting Appellees To Benefit From Another's Fraud Is At Variance With The Opinion Of The Supreme Court.

After the trial below and after the Federal District Court had appointed a receiver for Crateo's assets, evidence emerged that one debt for $293,647, constituting 40% of the claimed mature debt presented to the jury, had been founded by a bank upon a forged note.

Upon discovery of the fraud, a motion was forthwith made to the Court to perpetuate testimony. It was denied and appealed. Thereafter, the record of the Nevada Court, in which the fraud was set forth, was obtained and a motion for new trial based on the newly discovered fraud was made. It too was denied and appealed.

The Ninth Circuit, in the case below, stated:

> "The bank, however, was not a party in Crateo's bankruptcy proceeding. The Texas judgment was merely introduced into evidence by other creditors of Crateo as tending to show Crateo was unable to pay its debts as they matured. There is no indication that any of those petitioning creditors knew of any possible irregularities connected with the evidence. Despite Crateo's protestations of fraud in the obtaining of the Texas judgment its Rule 60(b) motion in this case cannot be considered as falling under the third clause of that section because the bank's actions cannot be charged to any adverse party in the bankruptcy proceeding."

The effect of the Ninth Circuit opinion is 40% of the claims found to be "mature" by the Master were not due at all; that 40% amounted to $293,697. Yet they are used to thrust Crateo into bankruptcy.

The magnitude of that fraud is shown when juxtaposed with the facts that (1) Crateo had over 800 vendor creditors who were constantly being paid (R.T. 292, lines 1-3) and (2) Crateo was paying its non-disputed debts as they matured (R.T. 282, line 2).

The decision of the Ninth Circuit, shielding the creditors in their use of a judgment tainted by fraud amounting to extrinsic fraud is directly contrary to the decision of this Court in *Hazel Atlas Co. v. Hartford Co.*, 322 U.S. 238, 88 LE 250, 64 S.Ct. 997 (1944).

Under the Supreme Court's thesis the District Court below had the power to act directly upon those beneficiaries of the fraudulent judgment who are asserting rights based upon it.

In *Hazel Atlas, supra,* this court noted the general rule that courts are reluctant to alter judgments after the expiration of the

term at which judgments are finally entered, but that there has always existed, along side the term rule, another equity rule that certain circumstances, one of which is after discovered fraud, relief will be granted. The court then stated, at page 245:

> "Where courts have invoked the power relief has taken several forms: Setting aside the judgment to permit a new trial, altering the terms of the judgment, or restraining the beneficiaries of the judgment from taking any benefit whatsoever from it."

This is a most important appropriate case for the application of the rule of *Hazel Atlas, supra.*

The decision in *Southern National Bank of Houston v. Tri-Financial* (Crateo) cited at 317 Fed.Supp. 1173 (July 29, 1973) Texas District Court, was on appeal when *Southern National Bank* suffered a judgment in the District Court in Nevada that the signature of the maker of the note, Toni Clark, was a forgery. Had this matter been revealed to the Texas District Court, or to the Fifth Circuit where the case against *Tri-Financial* (Crateo, Inc.) was pending upon appeal, the case could have been reopened and the issue of the forgery and collateral estoppel could have come before the Texas Court when the case was not yet final. The Bank, however, did not reveal it. The Bank's attorneys - officers of the court - did not reveal it to any court.

It is clear that the *Southern National Bank of Houston,* having concealed the Nevada adjudication of forgery, could not use the prior Texas judgment with impunity or assert it in involuntary bankruptcy proceedings. The finality of the Texas judgment is attributable to its scheme of concealment. But here the case is live and the matter can be corrected.

The beneficiaries of that judgment, the petitioning creditors below, are seeking to take advantage of *Houston National Bank's* concealment of the adjudication.

The conduct of respondents, now that the fraud has been revealed, is exactly that characterized by the California Supreme Court as:

> "Attempting to profit from the wrong of another." *Moyle v. Landers*, 78 Cal. 99, 20 P. 241, 12 A.S. 122 (1889).

V.

Due Process Is Denied By Requiring An Entity To Attack Newly Discovered Fraud In Another Forum When (1) The Entity In Receivership Is Not Now Controlled By The Real Parties In Interest; (2) The Assets To Mount The Litigation Are Not In Their Control; (3) Discretionary Approval Of Court To Litigate Must First Be Had; (4) The Party Concealing The Fraud Appeared In The Court Below; And (5) The Concealment Of Fraud Was In Fact Perpetuated On The Court Below.

The Ninth Circuit, in dealing with the attempt to set aside the fraud, stated:

> "Crateo's post-judgment collateral attack on the Texas judgment was brought in the wrong forum."

That Ninth Circuit opinion *denies* Crateo *due process* for the following reasons:

1. It conceptually refers to "Crateo" as an entity without distinguishing between the former "corporation" and the new "entity in receivership."

2. Crateo "in receivership" is not controlled by its officers or directors. It is now controlled by the receiver.

3. Section 11C of the Bankruptcy Act specifically provides:

> "A receiver or trustee may, with the approval of the court, be permitted to prosecute as receiver or trustee any suit commenced by the bankrupt. . . ."

The litigation in the forum suggested by the Ninth Circuit could not take place by the parties prosecuting this appeal (*i.e.* the real parties in interest - the directors-shareholders of Crateo) since they had no standing to appear in any court other than the court below after the appointment of a receiver. Though cloaked in the name "Crateo" in these proceedings, they have no standing to use that "cloak" in another forum. Only a receiver or trustee has that standing.

4. Economically speaking, the assets with which to prosecute an action in another forum are in the receiver's hands. The Parties before this court are denied the economic resources of Crateo to contest the fraud in another forum. Effective litigation cannot be mounted if control of funds is in the hands of a receiver.

5. An attorney for the bank appeared in the San Diego courtroom of the U. S. District Court and audited Crateo's proceedings. That attorney failed to notify the court of the Nevada adjudication of forgery.

The Order appointing the receiver for Crateo, dated August 20, 1973, specifically recites: ("Also present and indicating support for the petition were the following attorneys representing creditors of Crateo." (It then set forth the name of the attorney appearing for the bank and the fact that he represented the bank.)

There are all the earmarks of an "appearance" in (a) the form of the bank being present as a creditor and being represented by attorneys; (b) indicating support; (c) being named in the Order appointing the receiver; and (d) withholding information, while present, of the Nevada Court dismissal on the basis of forgery.

6. The fraud of concealment of the forgery was committed in the court below by attorneys for the bank.

VI.

Petitioner Was Deprived Of Its Statutory Right To A Jury Trial By A Reference To A Master Who Found Upon The Ultimate Issues Of The Case. This Is Directly Contrary To The Decision Of This Supreme Court.

Crateo, Inc. made a timely jury demand below. The District Court thereupon referred the matter to a master who found the basic ultimate issue in the case: Whether Crateo, Inc. had debts which it was unable to pay when they matured. That is directly contrary to the decision of this Court in *LaBuy v. Howes Leather Co.*, 352 U.S. 249, 1 LE2d 290, 77 S.C. 309 (1957).

Even worse, the Master was a judge in the same District, and an officer and arm of the Court. He therefore imposed an "aura" or "imprimatur" on the findings which an ordinary litigant simply cannot dispel, no matter how sound his facts.

The District Court then carefully directed the jury to such an extent that there was no real jury trial:

1. It informed the jury that the case was complicated and that a master had been appointed.

2. It admonished the jury not to take notes.

3. It stated it would furnish the Master's Report to them in the jury room.

4. It refused to permit cross examination of the Master.

5. It furnished the Master's Report in the jury room.

6. The Master was identified in that Report as a Judge in that District.

7. The Master's Report contained "findings" on the ultimate facts.

The statutory right to a jury trial here was hopelessly compromised in a prejudicial manner in that:

a. The use of a Master here was unwarranted. The facts were not unusually complicated for a jury to comprehend.

b. Crateo was denied the opportunity to offer evidence on the need for a Master. The appropriate procedure would have been to allow Crateo to examine the Master to show to the Court that the evidence given before him was not so complicated as to be beyond the comprehension of the jury. See Fifth Circuit case of *Boyd Callan, Inc. v. U.S.* 328 F.2d 505 (1964).

c. Where the court is justified in making a reference to a master, because of some complicated fact issues, that reference should be carefully guarded so as not to invade the judicial process any more than is necessary to resolve the complicated issues which required the reference in the first instance.

d. A master should not be a judge or referee in the same district since that casts him in a position akin to a God in the eyes of the jury.

e. Fairness requires that cross examination of the master be permitted.

f. The master should, under no circumstances, be permitted to resolve the ultimate issue.

g. Fairness requires that the jury not be given the results of the master in such a manner as to bear the imprimatur of the court; telling the jury not to take notes; the Judge, rather than Master, reading the report, thereby precluding observation of demeanor; giving the report (an official document) to the jury to be taken into the jury room; permitting the report to find on the

ultimate facts, appointing a brother judge in the same district to be the master; referring to the master as judge; refusing to permit the judge-master to be cross examined.

The foregoing totality of acts denied Crateo its statutory right to a jury trial as is provided for in Section 19A of the Bankruptcy Act (11 USC Sec. 42a).

It is contrary to the opinion of this court in *LaBuy v. Howes Leather Co., supra.*

VII.

The Ninth Circuit Opinion Has Given Rise To A Serious Question Of Statutory Interpretation Of The Phrase "Inability To Pay Debts As They Mature." It Used The Term "Fixed" In Dealing With Installments Not Yet Due. It Conflicts With The Second Circuit Which Holds That Installments Not Yet Due Are Not Mature.

Crateo and Intermark had stipulated to an installment judgment for $232,466 payable at the rate of $5,000 per month. A judgment lien was recorded against two properties. The stipulation provided (1) this is an installment judgment; and, (2) Intermark and Crateo were to use their "best efforts" to sell the properties at the appraised price. It was a "mixed" judgment of "installments" and "performance."

Thereafter, a dispute arose between Crateo and Intermark because the stipulation was uncertain as to how the appraiser was to be selected. One installment payment of $5,000 had been made. One installment of $5,000 had been withheld because of the dispute, and this one installment was due at the cleavage date of the creditors petition.

To avoid dispute, Crateo deeded the two properties to Intermark with instructions to sell for any sales price it could get, and apply the proceeds to the debt.

The Ninth Circuit, in dealing with Intermark debt, stated:

> "Intermark Investing, Inc. was a judgment creditor of Crateo's pursuant to a stipulated judgment.....Part of the judgment provided that two parcels of property.....would be sold and the proceeds of the sale applied to reduce Crateo's debt to Intermark. A dispute arose over the manner in which the properties were to be appraised.....This was essentially a dispute over the manner in which the judgment would be satisfied and cannot obscure the fact that Crateo's liability to Intermark had already been *fixed.*" *In re Trimble Co.*, 339 F.2d 828 at 844 (3rd Cir. 1964).

The Ninth Circuit opinion that the entire Intermark obligation was "fixed" imports a word not found in the Bankruptcy Act and gives rise to a question of the statutory interpretation of the phrase "inability to pay debts as they mature" found in 3a(5). It focuses attention on the entire obligation rather than upon the amount presently due.

The error in the Ninth Circuit's opinion is that the total amount of an installment note may be "fixed." But that is tangential. The real issue is that any installments which are "not due" are simply "not mature."

The Second Circuit in *Government of the Virgin Islands v. Brown* 221 F.2d 402 (1955) recognized that:

> "Maturity, when applied to commercial paper, means the time when the paper becomes due and demandable. . . ."
>
> "When a note is made payable in installments . . . such installments as have become due and deemed to have matured." (221 F.2d 402 at 405).

Moreover, the Intermark stipulated judgment further could not be "mature" since it was a *"mixed" judgment* of both *"installment money"* and *"performance"* in that each party was to use its "best efforts" to sell the property.

Intermark, in not (1) using the two grant deeds given it, or (2) not selling at an execution sale, did not use its "best efforts" to sell the property. It did not perform. Since Intermark did not perform, neither the entire judgment, nor any installment, was mature.

The Ninth Circuit erred in interpreting the Bankruptcy Act so as to separate out the money portion of the "mixed judgment" and state it was "fixed."

Further, Intermark could have either sold the properties using the deeds or levied execution and prepaid the installments on the judgment.

Intermark has never affirmatively contended that the properties on which it had judgment liens were not of substantial value. It waived its security in the two properties by only $500. (Finding III i of the Third Report). The implication is that the difference of $229,348 found owing by the Master ($229,848 minus $500) was fully secured, and, therefore, fully recoverable. There was also unrebutted testimony that the two properties had a net equity of at least $210,000.

The error of the Ninth Circuit in looking at the whole obligation rather than the "installment" which is due is also demonstrated in the Olympia Business Service note relative to which the Court stated.

> "Under a promissory note to Olympia Business Service, Inc., Crateo was obligated to pay $1,200 per month . . . appellant did not make the payments due July 1, 1970, and August 1, 1970 . . .

> whether or not Crateo received proper notice so as to accelerate payment of the entire amount remaining on the promissory note is irrelevant because the two monthly installments were definitely due at the time the creditors petition was filed."

By use of the wording "two monthly installments were definitely due at the time the creditors petition was filed," the Appellate Court implies, but does not say, that the Master's finding of a $90,000 obligation by Crateo to Olympia Business Service was overreaching. Crateo did not receive notice of acceleration of the note.

Crateo was denied a fair trial by:

1. Submitting the whole $232,466 Intermark judgment to the jury, rather than, at most, the one $5,000 withheld installment which was "mature"; and

2. Submitting the whole Olympia Business Service note for $90,000 to the jury rather than the two installments for $1,200 each which were due and mature.

The Second Circuit's position of "maturity" ought to prevail over the Ninth Circuit's tangential concept of using the word "fixed" since something can be "fixed," yet not be due at this time.

VIII.

The Ninth Circuit Decision Below, If Allowed To Stand, Will Destroy California's Statutory Scheme Of Voluntary Dissolution Of Corporation.

The only reason for a corporation in voluntary dissolution to go to the Superior Court is to obtain injunctive relief *against* would-be claimants for "claims and demands against the corporation, whether due or not yet due, contingent or unliquidated, or sounding only in damages." (Cal. Corp. Code 4608).

Crateo and many other companies that desire to voluntarily dissolve, have unliquidated claims against them. The only way of getting those claims eliminated or reduced to liquidated amounts is through this court process. In effect it: (a) funnels the claims into one court and (b) speeds up the time in which they must be presented. In essence, the statute permits litigation to take place in one place. It is a kind of "wholesale," "one location" approach as opposed to a "retail," "many situs" approach.

It is another mode of orderly adjustment with creditors as contemplated and permitted by the United States Supreme Court in *United States v. Kras*, 93 S.Ct. 631 at 640, 409 U.S. 434, 34 L.E2d 626 (1973).

As Chief Justice Burger therein stated:

> "The bankruptcy court is but one mode of orderly adjustment with creditors; it is not the only one since many debtors work out binding private adjustment with creditors." *United States v. Kras*, 93 S.Ct. 631 at 640, (1973) (concurring opinion).

If creditors can argue that by filing such a voluntary petition the directors are converted into trustees for creditors because of Bankruptcy Act Section 3a(5), then no corporation is going to be willing to risk using that California Statute.

This means that instead of a swift liquidation in one place, corporations will have to creep along until litigation is completed and the various Statutes of Limitation on claims have expired. This can take many years.

This simply is not efficient for the economy; it is against sound commercial practice; it freezes money and talent in a lingering corporate entity instead of permitting it to flow to new entities that can use that talent and money; it denies the shareholders the use of their investment for the duration of the long, drawn-out process.

It is not efficient for the judicial system. It proliferates and drags on litigation in many places.

CONCLUSION

1. The Ninth and Second Circuits differ on the need for an "appointment" of a "receiver" by "a court."

2. Converting directors into trustees or receivers for creditors creates serious Constitutional problems.

3. The Ninth Circuit conflicts with California Statute and the Eighth Circuit on the need for a disinterested party to be the trustee or receiver.

4. The Ninth Circuit conflicts with the Supreme Court on the issue of benefiting from another's fraud.

5. Due process was denied by requiring fraud upon the court below to be attacked in another forum.

6. The Ninth Circuit, contrary to Supreme Court decision, denied the right to a jury trial by referral to a Master-Judge who found on ultimate issues.

7. The Ninth Circuit conflicts with the Second Circuit on the issue of the "maturity" of installments not yet due.

8. The Ninth Circuit decision will destroy California's Statute for the dissolution of corporations.

This Court should grant Certiorari to resolve the magnitude of conflicts.

Respectfully submitted,

WALTER WENCKE
Attorney for Petitioner

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Of Counsel

APPENDIX

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

IN RE CRATEO, INC., Bankrupt.	FILED May 27, 1976 EMIL E. MELFI, JR. Clerk, U.S. Court of Appeals
CRATEO, INC., Appellant, vs. INTERMARK, INC., et al., APPELLEES.	Nos. 73-3208, 74-2088, 74-2615, and 75-3061 OPINION

Appeal from the United States District Court
for the Southern District of California

Before: KOELSCH and GOODWIN, Circuit Judges, and
WOLLENBERG* District Judge

WOLLENBERG, District Judge:

Crateo, Inc., a California corporation, was in the business of purchasing "sick" Companies. Its own health came into question in late summer of 1970, and its creditors initiated involuntary bankruptcy proceedings. After a jury trial on the question of its ability to pay its debts, Crateo was adjudicated a bankrupt.

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*Honorable Albert C. Wollenberg, United States District Judge, Northern District of California, sitting by designation.

While appeal from that judgment was pending, Crateo requested permission from the trial court to take depositions pursuant to Rule 27(b) of the Federal Rules of Civil Procedure. While its original appeal was still pending, Crateo also filed in the trial court two motions to vacate the adjudication of bankruptcy under Rule 60(b) of the Federal Rules of Civil Procedure. Appeals from the denial of all three post-judgment motions were consolidated with the primary appeal. 1/ Finding no merit in any of appellant's arguments, we affirm the adjudication of bankruptcy and decline to remand the case for any further proceedings.

I. Adjudication of Bankruptcy

In the summer of 1970, Crateo elected to wind up its affairs and voluntarily dissolve. On August 31, 1970, it filed a petition for judicial supervision of the winding up process with the Superior Court of the State of California for San Diego County. See California Corporations Code §4607. On that same day, the Superior Court ordered that notice of the dissolution proceeding be published and that all known creditors of Crateo be informed of the petition. In addition, the Superior Court ordered all creditor actions against Crateo enjoined and required all claims against Crateo to be presented in the dissolution proceedings. See California Corporations Code §§4608, 4616. Shortly thereafter, a creditors' petition was filed in the District Court alleging that Crateo had committed the fifth act of bankruptcy as defined by Section 3(a)(5) of the Bankruptcy act, 11 U.S.C. §21(a)(5).

1/

The appeal from the adjudication of bankruptcy is No. 73-3208. The appeal from the denial of permission to take post-judgment depositions is No. 74-2088. The appeals from the denials of the motions to vacate judgment are Nos. 74-2615 and 75-3061.

In accord with Section 19(a) of the Bankruptcy Act, 11 U.S.C. §42(a), Crateo requested a jury trial on the question of its insolvency. Prior to that trial, several issues, including the issue of Crateo's insolvency, were referred to the referee in bankruptcy sitting as a special master. The special master's report on the issue of Crateo's insolvency was read to the jury at trial. The jury subsequently found that Crateo was insolvent at the time it filed its petition for dissolution in the state court, and a judgment adjudicating Crateo a bankrupt was entered on August 9, 1973.

Appointment of a Receiver or Trustee

The petitioning creditors alleged that Crateo's petition in the state court for judicial supervision of its dissolution amounted to the fifth act of bankruptcy, 11 U.S.C. §21(a)(5). That section provides, in pertinent part, that:

> Acts of bankruptcy by a person shall consist of his having . . . (5) while insolvent or unable to pay his debts as they mature, procured, permitted or suffered voluntarily or involuntarily the appointment of a receiver or trustee to take charge of his property. 2/

California law governing the dissolution of corporations creates a significant change in the status of the corporation and its directors. We agree with appellant's creditors and the District Court that the net effect of this change means that Crateo's actions in the state court resulted in the "appointment of a receiver or trustee" within the meaning of 11 U.S.C. §21(a)(5).

2/

The definition of "persons" in 11 U.S.C. §1(23) makes this section applicable to corporations.

After a petition for dissolution is filed, the board of directors continues to operate the corporation in order to settle its affairs. Cal. Corp. Code §4800. However, directors may be removed by the superior court for reasons of "dishonesty, misconduct, neglect, or abuse of trust." Cal. Corp. Code §4614. The court can take such an action on its own initiative, and the normal prerequisite of a shareholder's suit is not required. *Cf.* Cal. Corp. Code §811.

The duties of the board of directors are also limited once the dissolution proceedings come under judicial supervision. The only business the corporation can carry on is that of winding up. Cal. Corp. Code §4605. In carrying out this task, the board of directors is invested with extensive powers. Cal. Corp. Code §4801. The powers of the board of directors, however, are not unlimited. The state court has the specific power to determine the manner in which claims are to be presented and settled and how shareholders' rights are to be determined. The court has the power to oversee the complete dissolution process and discharge the directors from their obligations after the process is completed. Cal. Corp. Code §§4608-11, 4617. In addition, the court has the general power to "make orders and adjudge as to any and all matters concerning the winding up of the affairs of the corporation." Cal. Corp. Code §4607.

In winding up the corporation's affairs, the first duty of the board of directors is to satisfy the corporation's debts and liabilities. Cal. Corp. Code §5000. In satisfying these obligations, the directors' powers under Cal. Corp. Code §4801 are circumscribed by the overall supervisory power of the Superior Court under Cal. Corp. Code §4607. If the directors do not settle the corporation's obligations properly, the court has the duty to vacate the directors' actions and to make the appropriate settlement itself. *In re Trinity Tractor Co.*, 3 Cal.App.3d 428, 440-441, 83 Cal.Rptr. 783, 791-792 (1970).

In addition, Crateo's creditors could no longer pursue their normal legal remedies against Crateo once the Superior Court accepted Crateo's petition for judicial supervision of its dissolution proceedings. Actions already begun were stayed by the Superior Court's order. Whether or not legal title to the corporation's assets passed into the possession of the board of directors became irrelevant because creditors could sue neither entity.

There was no need for the board of directors to be formally appointed trustees or to formally possess legal title to the corporation's assets. The effect of Crateo's actions in the Superior Court was to require its board of directors, under court supervision, to act as trustees. 3/ In determining whether a corporate dissolution under state law is the equivalent of the fifth act of bankruptcy, "it is the end result that counts." *In re Bonnie Classics,* 116 F.Supp. 646, 648 (S.D.N.Y. 1953). 4/

3/

This result is not changed by the additional possibility that a receiver may be appointed pursuant to California Code of Civil Procedure §§564, 565.

4/

Blair & Co., Inc. v. Foley, 471 F.2d 178 (2d Cir. 1972), *vacated and remanded for consideration of mootness*, 414 U.S. 212 (1973), is not to the contrary. That case involved a private arrangement between a brokerage firm and the New York Stock Exchange for the appointment of a liquidating agent for the firm. No court was involved in the liquidation process nor did the winding up process force creditors to forego their normal legal remedies. In light of the different factual situation herein, we need not comment further on the *Blair* case.

Not every corporate petition for dissolution under the California Corporations Code will necessarily result in an involuntary bankruptcy. Under 11 U.S.C. §21(a)(5), the creditors must also show that the debtor was "insolvent or unable to pay his debts as they mature." However, if this situation exists, California corporations cannot defeat the operation of the bankruptcy laws by applying for dissolution under California law. *In re Watts & Sachs*, 190 U.S. 1, 27 (1902). The overly technical approach to the interpretation of 11 U.S.C. §21(a)(5) urged by Crateo must be rejected.

Petitioning Creditors

The creditors' petition against Crateo was required by Section 59(b) of the Bankruptcy Act, 11 U.S.C. §95(b), to be filed by at least "three or more creditors who have provable claims not contingent as to liability." Six petitioning creditors 5/ presented evidence before the special master, and Crateo claims that none of them had claims "not contingent as to liability." Examination of the creditors' claims, however, shows that appellant is incorrect.

Intermark Investing Inc. was a judgment creditor of Crateo's pursuant to a stipulated judgment entered in a state court prior to the filing of the creditors' petition. Part of the judgment provided that two parcels of property owned by Crateo would be sold and the proceeds of the sale applied to reduce Crateo's debt to Intermark. A dispute arose over the manner in which the properties were to be appraised prior to their sale. This

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5/ Two of the original petitioning creditors and four intervening creditors presented evidence before the special master on this question. Under 11 U.S.C. §95(f), the intervening creditors took on the status of petitioning creditors. *3 Collier on Bankruptcy* ¶59.29 (14th ed. 1975).

was essentially a dispute over the manner in which the judgment would be satisfied and cannot obscure the fact that Crateo's liability to Intermark had already been fixed. *In re Trimble Co.*, 339 F.2d 838, 844 (3rd Cir. 1964).

Under a promissory note to Olympia Business Service, Inc., Crateo was obligated to pay $1200 per month. Since appellant did not make the payments due July 1, 1970, and August 1, 1970, Olympia was properly determined to be a creditor whose claim was not contingent as to liability. There was no need for Olympia to obtain a judgment against Crateo before it could achieve the status of a petitioning creditor under Section 59(b). *Denham v. Shellman Grain Elevator, Inc.*, 444 F.2d 1376, 1380 (5th Cir. 1971). Whether or not Crateo received proper notice so as to accelerate payment of the entire amount remaining on the promissory note is irrelevant because the two monthly installments were definitely due at the time the creditors' petition was filed.

General Electric Company held two promissory notes which had fully matured prior to August 31, 1970. Again, there was no need for General Electric to have obtained judgments on these notes in order to satisfy the requirements of Section 59(b). The fact that there was a dispute over Crateo's indebtedness on another separate obligation to General Electric is irrelevant. 6/

Use of Special Master's Report at Jury Trial

Under Section 19(a) of the Bankruptcy Act, 11 U.S.C. §42(a), Crateo was entitled to a jury trial "in respect to the

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6/ While it would not be helpful to discuss the claims of the three other petitioning creditors, we believe the District Court correctly held that their claims were not contingent as to liability.

question of [its] insolvency." 7/ Prior to that trial, the issue of Crateo's insolvency had been referred to the referee in bankruptcy sitting as a special master. The report of the special master was then read to the jury pursuant to Rule 53(e)(3) of the Federal Rules of Civil Procedure. Crateo contends that the procedure followed in this case violated its right to a trial by jury on the question of its insolvency.

Crateo first claims that reference to a special master was unwarranted because the issues were readily understandable by a jury. F.R.C.P. Rule 53(b) provides that "in actions to be tried to a jury, a reference shall be made only when the issues are complicated." 8/ The petitioning creditors had alleged that Crateo was bankrupt because it could not pay its debts as they matured. While every claim of this type does not require use of a master, considering Crateo's tangled financial affairs and the duplication of those problems in two subsidiary corporations that had been merged into Crateo three days before the filing

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Although 11 U.S.C. §42(a) also gives debtors the right to a jury trial on the question of whether they committed an act of bankruptcy, there was no need for a jury trial on that issue in this case. Crateo did not dispute the fact that it had filed a petition for judicial supervision of dissolution in the state court. Crateo only disputed the legal effect that could be attached to its action.

8/

The trial was held in June of 1973. General Order in Bankruptcy No. 37 was in effect at that time and made Rule 53 of the Federal Rules of Civil Procedure applicable to jury trials in bankruptcy cases. *Cf. Diamond Door Co. v. Lane-Stanton Lumber Co.*, 505 F.2d 1199 (9th Cir. 1974). The Federal Rules of Civil Procedure with respect to masters now apply to bankruptcy proceedings because of Bankruptcy Rule 513.

of the petition in state court for judicial supervision of dissolution, we believe that there was no abuse of discretion in reference to the special master. Since this was a matter for the district judge's determination in light of his perception of whether the jury would find the issue complicated, Crateo's request to examine the special master on the complexity of the case was properly denied.

At the trial, the findings of the special master were read to the jury. In providing that these findings are "admissible as evidence" and "may be read to the jury," Rule 53(e)(3) does not require the special master to personally read the findings to the jury. Consequently, contrary to appellant's position, the special master did not have to be made available for cross examination on the procedures used to reach the findings presented to the jury.

The expert qualifications of the special master were Crateo's primary guarantee that the proper legal standards and procedures were used by the master in determining his findings. In this respect, it is significant that Crateo did not object to the qualifications of the master appointed in this case. 9/ At the trial, Crateo was given a full opportunity to introduce evidence that would contradict the findings of the special master and argue to the jury that the findings were incorrect. The jury was instructed on the role of the special master and the weight to be given to his report, and Crateo did not object to this instruction.

The procedures employed in the trial would not impermissibly interfere with the right to trial by jury guaranteed by the Seventh Amendment. *Ex parte Peterson*, 253 U.S. 300 (1920);

9/

Crateo was not prejudiced by the fact that the special master happened to be a federal bankruptcy referee.

Burgess v. Williams, 302 F.2d 91 (4th Cir. 1962). Crateo's statutory right to a jury trial under the Bankruptcy Act gives it no greater rights than those available in civil proceedings governed by the Seventh Amendment. *Diamond Door Co. v. Lane-Stanton Lumber Co.*, 505 F.2d 1199 (9th Cir. 1974). Under all the circumstances of this case, we conclude that Crateo received a fair and proper trial on the question of its insolvency.

Jury Instructions

The petitioning creditors had alleged and were required to prove that Crateo was "unable to pay [its] debts as they mature" when it petitioned for a judicially supervised dissolution in state court. 11 U.S.C. §21(a)(5). This is the "equity" definition of insolvency. The trial judge's instruction to the jury followed the language of the statute. 10/ Crateo objected to this instruction, claiming that the word "debts" is in the plural and therefore the creditor must show the debtor's inability to pay "substantially all" of its debts and not just the debtor's inability to pay "one or two or three" debts.

The words "unable to pay [its] debts as they mature" are contained in a statutory context which necessitates rejection of Crateo's argument. A debtor commits the fifth act of bankruptcy when he is unable to pay his debts as they mature *and* a receiver or trustee is appointed to take charge of his property. 11/

10/ The jury was instructed that "considering only those items which you have concluded are both debts and are mature, you must decide whether Crateo, Inc. had the ability to pay these debts on August 31, 1970."

11/ Thus, contrary to the implications in Crateo's argument, debtors are not thrown into bankruptcy merely because they cannot pay a few small debts at a particular moment.

In that situation, there is a good possibility that some creditors may not be able to recover their claims on an equitable basis with other creditors unless they are able to invoke the protections of the Bankruptcy Act. Without those protections, the fact that some, or even most, of the creditors could be paid is of little consolation to those who cannot be paid. Adoption of Crateo's position would be completely contrary to the increasing amount of protection afforded to creditors by successive revisions of 11 U.S.C. §21(a)(5). 12/ In addition, Crateo's proposed test would be so indefinite as to be unworkable. The trial judge properly declined to modify his instructions.

II. Motions to Vacate the Adjudication of Bankruptcy

Approximately eight months after judgment was entered adjudicating Crateo to be a bankrupt, and while the appeal from the judgment was pending, Crateo filed a motion in the District Court to vacate the judgment under Rule 60(b) of the Federal Rules of Civil Procedure. Because of the pending appeal, the District Court had no jurisdiction to enter an order under Rule 60(b). The most the District Court could do was to either indicate that it would "entertain" such a motion or indicate that it would grant such a motion. If appellant had received such an indication, its next step would have been to apply to this Court for a remand. *Canadian Ingersoll-Rand Co. v. Peterson Products*, 350 F.2d 18, 27-28 (9th Cir. 1965).

In this case, however, the District Court found that it was inappropriate to either grant or entertain the Rule 60(b) motion. This was only a procedural ruling and not a final determination of the merits of the Rule 60(b) motion. Such an order is not appealable. Crateo's "appeal" from the District Court's order

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12/ See 1 *Collier on Bankruptcy* ¶3.501 (14th ed. 1974).

must therefore be considered as a motion for remand of the case for consideration of the Rule 60(b) motion. *Weiss v. Hunna*, 312 F.2d 711, 713 (2d Cir. 1963) *cert. denied*, 374 U.S. 753 (1963); *Canadian Ingersoll-Rand Co. v. Peterson Products, supra*, 350 F.2d at 27 n. 16. We decline to order such a remand.

The basis of Crateo's motion was an attack upon the validity of a judgment from the United States District Court for the Southern District of Texas in favor of the Southern National Bank of Houston and against Crateo. See *Southern National Bank of Houston v. Tri Financial Corporation*, 317 F.Supp. 1173 (S.D. Tex. 1970), *affirmed sub nom. Southern National Bank of Houston v. Crateo, Inc.*, 458 F.2d 688 (5th Cir. 1972). This judgment was introduced as evidence tending to prove that Crateo was unable to pay its debts as they matured and comprised a large proportion of Crateo's unpaid debts. In its Rule 60(b) motion, Crateo claimed that the Texas judgment was obtained by fraud and should not have been considered at Crateo's bankruptcy trial.

The District Court in Texas had determined that Tri Financial, a predecessor of Crateo, was obligated to purchase a promissory note from the bank. While that decision was on appeal to the Fifth Circuit, the bank brought an action against one of the signers of the note in the United States District Court for the District of Nevada. After the defendant in the Nevada action raised the claim that her signature on the note had been forged, the bank decided not to prosecute its suit and the case was dismissed. The Fifth Circuit's decision came after the events in Nevada.

The bank, however, was not a party in Crateo's bankruptcy proceeding. The Texas judgment was merely introduced into evidence by other creditors of Crateo as tending to show Crateo was unable to pay its debts as they matured. There is no indication that any of those petitioning creditors knew of any possible irregularities connected with the evidence. Despite

Crateo's protestations of fraud in the obtaining of the Texas judgment, its Rule 60(b) motion in this case cannot be considered as falling under the third clause of that section because the bank's actions cannot be charged to any adverse party in the bankruptcy proceeding. 13/

The jurisdiction of the District Court in Texas over the parties in *Southern National Bank of Houston v. Tri Financial Corporation, supra*, was not challenged in the bankruptcy proceedings, and the petitioning creditors were entitled to rely on the judgment's presumptive validity. Crateo's post-judgment collateral attack on the Texas judgment was brought in the wrong forum. 14/

In its Rule 60(b) motion, Crateo also claimed that the bank had received some payments on the promissory note and that Crateo's indebtedness to the bank was therefore less than

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13/ Assuming that the inability to collect from one of the alleged signers of the promissory note eliminated Tri Financial's obligation to purchase the note from the bank, any possible fraudulent conduct in this situation would consist of the bank not informing the Fifth Circuit of the invalidity of the obligation before it affirmed the judgment of the District Court in Texas.

14/ The bank's Nevada action terminated in June of 1971, and the trial on the issue of Crateo's insolvency did not take place until June of 1973. Crateo first raised this issue in early 1974 when it moved for an order perpetuating testimony pending appeal. No satisfactory explanation of the delay in producing evidence of the Nevada action is provided. The possibility that it may have been too late to petition either the Fifth Circuit or the District Court in Texas to set aside their judgments does not allow Crateo to collaterally attack the judgment in this proceeding.

the amount stated in the Texas judgment. Again, the collateral attack on a presumptively valid judgment was brought in the wrong forum.

We also decline to remand the case because of Crateo's second Rule 60(b) motion. All of the pertinent information that is the basis for this motion should have been known to Crateo well before the 1973 trial on the issue of its insolvency. There is no excuse for waiting over two years after entry of judgment before filing this motion. 15/

III. Perpetuation of Testimony Pending Appeal

While the appeal from the adjudication of bankruptcy was pending, Crateo requested permission, pursuant to Rule 27(b) of the Federal Rules of Civil Procedure, to depose an officer of the Southern National Bank of Houston. This testimony was allegedly needed to investigate the circumstances surrounding the purported forgery on the promissory note and the satisfaction of the note discussed in part II, *supra*. The order denying Crateo's motion is an appealable order. *Ash v. Cort*, 512 F.2d 909 (3rd Cir. 1975). *Cf. Martin v. Reynolds Metals Corporation*, 297 F.2d 49 (9th Cir. 1961).

On appeal, we must decide whether there was an abuse of discretion by the trial court. *Ash v. Cort, supra.* For the reasons stated previously in part II, *supra*, Crateo could not collaterally attack the Texas judgment. There was, therefore, no reason in this bankruptcy proceeding to take depositions on the subject. Crateo's motion was properly denied.

15/ Many of the arguments raised by Crateo with respect to these two Rule 60(b) motions are irrelevant to the motions and are attempts to reargue the primary appeal. This is not the proper function of a Rule 60(b) motion.

The judgment in No. 73-3208 and the order in No. 74-2088 are affirmed. The appeals in Nos. 74-2615 and 75-3061 are dismissed. Considering Nos. 74-2615 and 75-3061 as motions to remand to permit the district judge to consider appellant's Rule 60(b) motions, the motions are denied.

No. 76-226

In the Supreme Court of the United States

OCTOBER TERM, 1976

In re CRATEO, INC.,

Bankrupt,

CRATEO, INC.,

Petitioner,

v.

INTERMARK, INC., et al.,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR
WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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TOPICAL INDEX

TOPICAL INDEX (Continued)

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES (Continued)

[The relevant portions of these statutes and rules are set forth in full in Appendix B.]

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1976

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The Respondents, Intermark, Inc., et al., respectfully pray that the United States Supreme Court deny the petition of Crateo, Inc. ("Crateo") for a Writ of Certiorari to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit.

OPINION BELOW

The opinion of the Court of Appeals for the Ninth Circuit is reported at 536 F.2d 862 and is contained in Appendix A. No written opinion was rendered by the District Court. However, it adopted the written opinion of the Special Master, who had been appointed by the District Court.

JURISDICTION

The opinion and judgment of the United States Court of Appeals for the Ninth Circuit was entered on May 27, 1976, affirming a judgment of the United States District Court for the Southern District of California dated August 7, 1973. The United States Court of Appeals for the Ninth Circuit denied a petition for rehearing on June 28, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

STATUTORY PROVISION INVOLVED

Bankruptcy Act Section 3a(5) [11 U.S.C. Section 21a(5)]:

> "a. Acts of bankruptcy by a person shall consist of his having. . . .
>
> (5) while insolvent or unable to pay his debts as they mature, procured, permitted, or suffered voluntarily or involuntarily the appointment of a receiver to take charge of his property."

QUESTIONS PRESENTED

1. Did Crateo, a corporation, commit the fifth act of bankruptcy within the meaning of Section 3a(5) of the Bankruptcy Act: (1) by filing a petition for judicial supervision of the winding up of its affairs pursuant to Sections 4607 and 4616 of the

California Corporations Code; (2) where the state Superior Court stayed all actions by creditors against Crateo and required its creditors' claims to be proved and presented to the Superior Court; and (3) where a jury determined that Crateo was unable to pay its debts as they matured?

2. Does a holding that the actions listed in Question 1 constitute the fifth act of bankruptcy in any way violate the constitutional rights of Crateo's directors or shareholders, or does it deny Crateo's creditors the protection they are to be afforded under the Bankruptcy Act?

3. Did the Ninth Circuit Court of Appeals error in considering Crateo's liability on the Texas judgment relevant to Crateo's ability to pay its debts as they matured, even though Crateo alleged that the judgment was subject to attack for extrinsic fraud?

4. Did the Ninth Circuit Court of Appeals error in refusing to allow Crateo to collaterally attack, for alleged extrinsic fraud, a judgment rendered in the Southern District of Texas and affirmed by the United States Court of Appeals for the Fifth Circuit where: (1) Crateo had not sought to set aside the judgment in the Court which rendered the judgment, and (2) where Crateo could offer no satisfactory explanation for its failure to raise the issue of the alleged extrinsic fraud for over two years?

5. Was the statutory right to a jury trial denied to Crateo where a Special Master was appointed to evaluate the complex financial situation of the bankrupt pursuant to Federal Rule 53; where the findings of the Special Master were read to the jury by the Judge; and where Crateo did not object to the use of the Special Master until after the Special Master had made a determination of preliminary issues adverse to the Petitioner?

6. Is liability on a stipulated judgment a "fixed liability," and thus a provable claim within the meaning of Section 63(a) of the Bankruptcy Act?

STATEMENT OF THE CASE

This case involves an involuntary bankruptcy proceeding brought by a number of creditors to have the Petitioner, Crateo, a California corporation, adjudicated a bankrupt. The Respondent petitioning creditors have heretofore successfully asserted that Crateo committed the fifth act of bankruptcy set forth in Section 3a(5) of the Bankruptcy Act [11 U.S.C. Section 21(a)(5). Hereinafter referred to merely as "Section 3a(5) of the Bankruptcy Act."] and should be adjudicated a bankrupt.

On August 31, 1970, Crateo filed with the San Diego County Superior Court a Petition for Judicial Supervision of the Winding Up of its affairs pursuant to the provisions of Sections 4607 and 4616 of the California Corporations Code. Crateo's Petition alleged that it was subject to a great volume of litigation from creditors and it sought the Superior Court's umbrella of protection in the form of a stay of existing lawsuits and an order requiring creditors to file claims in the dissolution proceeding. On the same day, the Superior Court issued its order requiring all creditors to submit claims to the Court's clerk on or before March 30, 1971. The order also provided as follows:

> "All creditors and claimants against Crateo, Inc., are hereby enjoined and stayed from prosecuting any suit, proceeding, or action against Crateo, Inc., and are required to present and prove their claims in the manner required of creditors."

All persons with claims against Crateo were thus foreclosed from pursuing their normal remedies against Crateo and were required to appear and present their claims to the Superior Court.

The creditors' petition was filed on September 18, 1970, and an amended petition was filed on September 21, 1970.

Crateo filed its answer and demanded a jury trial. Because the proceeding involved complex issues of fact and law, on May 24, 1971, the Honorable Howard B. Turrentine, United States District Court Judge, appointed Charles M. Fox, Jr., a Referee in Bankruptcy, to sit as a Special Master in accordance with Rule 53 of the Federal Rules of Civil Procedure. Referee Fox held a number of hearings during which evidence was received and thereafter submitted to the District Court four reports, all favorable to petitioning creditors' positions. Judge Turrentine, after considering Crateo's objections, adopted the first three reports which dealt with non-jury issues. Portions of the fourth report were read into evidence by Judge Turrentine at the jury trial. On June 13, 1973, the jury returned a verdict that Crateo was unable to pay its debts as they matured as of August 31, 1970. A judgment adjudicating Crateo a bankrupt was entered on August 9, 1973. Crateo appealed this judgment to the Ninth Circuit Court of Appeals [No. 73-3208].

After filing an appeal with the Ninth Circuit Court of Appeals from the District Court's decision adjudicating it a bankrupt, Crateo filed a motion in the District Court pursuant to Rule 27(b) of the Federal Rules of Civil Procedure requesting leave to take depositions to perpetuate testimony pending appeal. The District Court denied that motion [No. 74-2088] and an appeal of that denial was docketed with the Ninth Circuit Court of Appeals as No. 74-2088. Subsequently, on April 4, 1974, Crateo filed a motion with the District Court designated "Motion to Set Aside Judgment Based on Newly Discovered Evidence" [F.R.C.P. Rule 60(b)]. [No. 74-2615]. The motion was denied by the District Court and appeal No. 74-2615 followed. On May 27, 1976, the Ninth Circuit Court of Appeals affirmed all of the decisions of the District Court which Crateo had appealed.

REASONS WHY THIS COURT SHOULD DENY THE WRIT

Rule 19 of this Court sets forth the character of reasons which will be considered by it in reviewing on a Petition for a Writ of Certiorari. Petitioner argues in its petition that this case presents factors which justify such a review. As the discussion which follows will conclusively demonstrate, none of the special and important reasons set forth in Rule 19 for a review on Writ of Certiorari are herein present; the United States District Court for the Southern District of California and the Ninth Circuit Court of Appeals have examined this case in great detail, and have ruled correctly on all of the issues presented. Therefore, a review of this case on Writ of Certiorari by this Court would be inappropriate. Respondent sets forth the reasons why the assertions of Crateo are without merit and the reasons why these assertions do not satisfy the criteria of Rule 19 for review on Writ of Certiorari.

I

There is No Conflict Between the Ninth and Second Circuits Over What Constitutes the Fifth Act of Bankruptcy.

Petitioner has attempted to characterize a conflict between the decision in *Blair & Co., Inc. v. Foley*, 471 F.2d 178 (2d Cir. 1972), *vacated and remanded for consideration of mootness*, 414 U.S. 212, 94 S.Ct. 405, 38 L.Ed.2d 422 (1973), and the decision of the Ninth Circuit Court of Appeals here. As the citation to *Blair* indicates, the Second Circuit decision was vacated by this Court and, having been vacated, cannot be considered to conflict with the Ninth Circuit decision here. In any event, the Second Circuit decision in *Blair* is consistent with the Ninth Circuit's decision here. Both cases dealt with the question of what constitutes the fifth act of bankruptcy within the meaning of Section 3a(5) of the Bankruptcy Act. *Blair* involved the

question of whether the fifth act of bankruptcy had taken place by the appointment of a "liquidator" for Blair & Co., Inc. pursuant to an agreement between it, the New York Stock Exchange and others. The Liquidator was appointed pursuant to a *private agreement* and was authorized to take control of the business and property of Blair for the purpose of its liquidation. The Liquidator was not endowed with the authority to restrain creditors nor to adjudicate claims of creditors. The liquidation process was an informal one worked out by Blair and the New York Stock Exchange; Blair's creditors were not parties to nor bound by the agreement.

The circumstances of the instant case were significantly different: Crateo sought the aid of California's dissolution statutes and requested and received Court supervision and protection of the dissolution process. Crateo's creditors were enjoined from pursuing their normal remedies and instead were forced to present and prove their claims before the Superior Court. Moreover, in winding up Crateo's affairs, the first duty of its directors became satisfying the corporation's debts and liabilities. Calif. Corp. Code Section 5000.

The Ninth Circuit Court of Appeals considered the private arrangement examined in *Blair* clearly distinguishable from the Court supervised dissolution proceeding here:

> "*Blair & Co., Inc. v. Foley* . . . is not to the contrary. That case involved a private arrangement between a brokerage firm and the New York Stock Exchange for the appointment of a liquidating agent for the firm. *No Court was involved in the liquidation process nor did the winding up process force creditors to forego their normal legal remedies. In light of the different factual situations herein, we*

need not comment further on the Blair case." (536 F.2d at 866, n. 4. Emphasis added.)

Moreover, the Second Circuit in *Blair* explicitly recognized the significance of a Court supervised dissolution proceeding to the fifth act of Bankruptcy by observing the "obvious correctness" of the decision in *In re Bonnie Classics, Inc.*, 116 F.Supp. 646 (S.D.N.Y. 1953). The court in *In re Bonnie Classics* had held that the filing of a certificate of dissolution with the state Court under the then Section 105 of the New York Stock Corporation Law was an act of bankruptcy under Section 3a(5). (See *Blair* at 471 F.2d 178, 181.)

To summarize, even assuming the viability of the Second Circuit's decision in *Blair*, there is no conflict between the Second and Ninth Circuit Courts of Appeal as to that which constitutes the fifth act of bankruptcy. Neither Court has held that a private arrangement between the debtor and creditors satisfies Section 3a(5). However, both Circuits have recognized that a state Court supervised dissolution proceeding can constitute the fifth act of bankruptcy. The decision of the Second Circuit in *Blair* suggests that its decision in the instant case would have been identical to that of the Ninth Circuit.

II

The Decision of the Ninth Circuit Finding Crateo's Voluntary Invocation of the State Corporate Dissolution Scheme to be Tantamount to the Appointment of a Receiver or Trustee Within the Meaning of Section 3a(5) of the Bankruptcy Act Raises No Significant Constitutional Issue.

Crateo has sought to characterize the decision of the Ninth Circuit as "imposing" duties upon its directors and as "depriving" rights of its shareholders without their receiving notice and a hearing. This characterization is a total misdescription of the nature of the actions taken by Crateo through its board of directors. Moreover, Crateo did not raise this argument in the Courts below, and thus this Court should not consider it for that reason -- "We cannot decide issues raised for the first time here." *Tacon v. Arizona*, 410 U.S. 351, 352, 35 L.Ed.2d 346, 93 S.Ct. 998 (1973).

It is important to note that the Ninth Circuit did not impose duties upon the directors, they did so themselves by *voluntarily* seeking the aid of the Superior Court and California's corporation dissolution scheme. It was the invoking of this judicial and statutory protection by Crateo which the Ninth Circuit analyzed in concluding that the circumstances and the duties under state law to which Crateo's directors had voluntarily become subject were tantamount to the appointment of a trustee or receiver within the meaning of Section 3a(5) of the Bankruptcy Act.

Once it is understood that Crateo's directors and shareholders voluntarily assumed certain duties under State law in return for certain statutory and judicial benefits, it becomes clear that the subsidiary contentions of Crateo in its second argument are insubstantial and without merit:

1. Crateo's directors' fiduciary duties to its creditors were not imposed upon the directors without due process, because the directors themselves created any new duties they had to the creditors by *voluntarily* filing the petition for dissolution and seeking court protection.

2. Crateo's directors were not forced into the involuntary servitude of its creditors, because the directors *voluntarily* filed the petition for dissolution and thereby *voluntarily* assumed any new duties they had under state law to the corporation's creditors.

3. Crateo's shareholders were not deprived of control of the corporation without due process, because the directors, on the shareholders' behalf, voluntarily instituted the dissolution proceedings.

4. Crateo gratuitously seeks to allege on behalf of the Respondent creditors herein that the creditors' statutory right to appoint the trustee in bankruptcy was violated. The creditors have, of course, been attempting for the past six years to have Crateo finally adjudicated a bankrupt so that, among other things, an independent trustee in bankruptcy could be appointed. Crateo's argument on this point confuses the term "trustee" as used in Section 3a(5) with the term "trustee" in bankruptcy as used in Section 44 (11 U.S.C. Section 72).

Also important is the fact that Crateo has no standing to assert an alleged violation of Respondent's rights and thus Crateo's contentions under its second argument should not be considered for this reason. *NAACP v. Alabama*, 357 U.S. 449, 459, 2 L.Ed.2d 1488, 1497-1498, 78 S.Ct. 1163 (1958); *Griswold v. Connecticut*, 381 U.S. 479, 481, 14 L.Ed.2d 510, 512-513, 85 S.Ct. 1678 (1965).

5. Crateo's directors were not placed in civil jeopardy for violation of state law. The California Civil Code and the

relevant provisions of the California Corporations Code must be read together. Obviously, if the directors were acting in accordance with the Corporations Code and with the blessing of the Superior Court, they would not be deemed to be violating the California Civil Code. Moreover, this alleged inconsistency between California statutes obviously does not present an important question for Supreme Court review within the scope of Rule 19.

III

The Ninth Circuit Court of Appeal's Decision Here Does Not Conflict with the Decision of the Eighth Circuit Regarding a Disinterested Trustee.

In *R. J. Reynolds Tobacco Company, et al. v. A. B. Jones Co., Inc., et al.*, 54 F.2d 329 (1931) the Eighth Circuit Court of Appeals held that the determination of whether a receiver was suitable or not was within the discretion of the bankruptcy court. The underlying theory of the Court there was that the creditors were entitled to have an impartial trustee so that their rights would be protected. Here, the policy objective articulated in *R. J. Reynolds* was satisfied, because of the strict supervisory powers of the Superior Court during the dissolution proceeding and because Crateo's directors had a primary duty to its creditors.

Crateo again confuses the concept of a "trustee" as used in Section 3a(5) with the concept of "trustee" in bankruptcy as used in Section 44 of the Bankruptcy Act [11 U.S.C. Section 72]. *R. J. Reynolds Tobacco Co.'s* discussion of a disinterested "receiver" was in the context of the type of functions contemplated under Section 44. That case did not discuss the functions of a disinterested receiver within the meaning of Section 3a(5) of the Bankruptcy Act.

The Court should note that through Crateo's third argument, it again seeks to gratuitously assert the rights of the

Respondents rather than its own, and again it is clear that Crateo is without standing to do so. *NAACP v. Alabama*, 357 U.S. 449, 459, 2 L.Ed.2d 1488, 1497-1498, 78 S.Ct. 1163 (1958), *Griswold v. Connecticut*, 381 U.S. 479, 481, 14 L.Ed.2d 510, 512-513, 85 S.Ct. 1678 (1965). Also, Crateo did not raise this third argument in the Courts below, and thus for that reason this Court should not consider it. *Tacon v. Arizona, supra.*

IV

The Ninth Circuit Court of Appeal's Decision Denying Crateo's Motion to Collaterally Attack the Judgment of the District Court in Texas Did Not Violate the Rule Set Forth in Hazel Atlas Co. v. Hartford Co.

Crateo argues that the Ninth Circuit has allowed Respondents to benefit from another's fraud, and that by so doing the Ninth Circuit has violated the principle set forth in *Hazel Atlas Co. v. Hartford Co.*, 322 U.S. 238, 88 Law Ed. 250, 64 S.Ct. 997 (1944). That case involved the power of a Circuit Court, upon proof that fraud was perpetrated on *it* by a successful litigant, to vacate its own judgment entered at a prior term. The Supreme Court there held that in certain circumstances a Circuit Court of Appeals does have such power. The Court stated, however, that this power must be used cautiously because of the salutary rule that in most instances society is best served by putting an end to litigation after a case has been tried and judgment entered.

The rule of *Hazel Atlas* is not apposite in the instant case: Crateo did not ask the Ninth Circuit Court of Appeals to overturn a judgment rendered in *its Circuit* which had been allegedly procured by fraud. Crateo asked the Ninth Circuit to overturn *another* Circuit's judgment. The Ninth Circuit refused, finding that Crateo had come to the wrong forum. Moreover, Crateo

could not explain satisfactorily the reason for its delay of two and a half years in raising the issue of the use of alleged extrinsic fraud in procuring the judgment.

V

Petitioner Was Not Denied Due Process By Being Required To Attack The Texas Judgment In The Texas Rendering Court.

An argument that due process is violated by requiring a litigant to attack a judgment procured by alleged extrinsic fraud in the rendering court strains credulity. It is usually the rendering court which is most familiar with the facts of the case, and it is the rendering court which has the strongest interest in ensuring that fraud has not been perpetrated upon it. The Ninth Circuit's decision requiring Crateo to go to the rendering court to attack the judgment not only comported with fundamental notions of fair play, but it was clearly the most appropriate disposition of the matter.

Again Crateo seeks to assert an argument it did not raise in the Courts below, and thus again this Court should refuse to consider it.

VI

The Use Of A Special Master Pursuant To Rule 53 Of The Federal Rules Of Civil Procedure Did Not Impair Crateo's Statutory Right To A Jury Trial.

Crateo contends that the appointment of the Special Master and the reading of his report to the jury impaired its right to a jury trial as granted by the Bankruptcy Act in Section 19(a) [11 U.S.C. Section 42a]. By acquiescing in the appointment of the Special Master and by participating in proceedings

beforehand prior to raising any objections, Crateo waived any basis it may have had to object to the reference. In any event, the complexity of the case dictated the appointment of the Special Master. Crateo's attack is, in essence, an attack on the entire concept of a Special Master and would require the overruling of well established authorities sanctioning the use of Special Masters in jury trials. *E.g., In re Peterson,* 253 U.S. 300, 64 L.Ed. 919, 40 S.Ct. 543 (1920).

Crateo also contends that the District Court erred in reading the Special Master's report itself rather than having the Special Master read his own report. Rule 53(e)(3) makes clear that the Special Master's findings "may be read to the jury"; there is no requirement that the findings be read by the Special Master himself.

VII

The Ninth Circuit's Opinion Has Not Given Rise To A Serious Question Of Statutory Interpretation Regarding The Phrase "Inability To Pay Debts As They Mature."

Intermark Investing Inc. was a judgment creditor of Crateo's pursuant to a stipulated judgment entered in a state court prior to the filing of the creditors' petition. Part of the judgment provided that two parcels of property owned by Crateo would be sold and the proceeds of the sale applied to reduce Crateo's debts to Intermark. A dispute allegedly arose over the manner in which the properties were to be appraised prior to their sale. The Ninth Circuit found that:

> "This was essentially a dispute over the manner in which the judgment would be satisfied and cannot obscure the fact that Crateo's liability to Intermark had already become *fixed. In re Trimble Co.,* 339 F.2d 828, 844 (3rd Cir. 1964)". (536 F.2d at 867. Emphasis added.)

The Ninth Circuit here was obviously holding that Crateo had a "fixed liability" to Intermark within the meaning of Section 63(a) of the Bankruptcy Act [11 U.S.C. Section 103a]. Intermark's claim against Crateo was thus "provable" and hence Intermark qualified as a creditor which could petition for an involuntary bankruptcy of Crateo under Section 59(b) of the Bankruptcy Act [11 U.S.C. Section 95b]. This logical statutory interpretation, which was consistent with *In re Trimble Co.* cited by the Ninth Circuit, clearly raises no serious question of statutory interpretation and is not in conflict with decisions of the Second Circuit.

VIII

The Ninth Circuit's Decision Below, If Allowed To Stand, Will Not Destroy California's Statutory Scheme Of Voluntary Dissolution Of Corporations.

The Ninth Circuit's opinion effectively refutes the eighth argument in Crateo's petition:

> "Not every corporate petition for dissolution under the California Corporations Code will necessarily result in an involuntary bankruptcy. Under 11 U.S.C. Section 21(a)(5), the creditors must also show that the debtor was 'insolvent or unable to pay his debts as they mature.' *However, if this situation exists, California Corporations cannot defeat the operations of the bankruptcy laws by applying for dissolution under California law. In re Watts and Sachs,* 190 U.S. 1, 27 (1902). The overly technical approach to the interpretation of 11 U.S.C. Section 21(a)(5) urged by Crateo must be rejected." (536 F.2d at 866-867. Emphasis added.)

CONCLUSION

The relevant legal issues presented in this case have, over the past six years, been explored fully by the Special Master, the United States District Court for the Southern District of California, and the Ninth Circuit Court of Appeals. After a detailed examination of these issues, these tribunals have appropriately found the relevant contentions raised by Crateo in its instant petition to be without merit. A reading of Crateo's petition and this brief in opposition thereto conclusively demonstrates that Crateo has not set forth any appropriate reasons for a review of this case on Writ of Certiorari by this Court.

Therefore, this Court should refuse to grant the Writ of Certiorari for which Crateo has petitioned.

Respectfully submitted,

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APPENDICES

A-1

In re Crateo, Inc., Bankrupt.

CRATEO, INC., Appellant,

v.

INTERMARK, INC., et al., Appellees.

Nos. 73-3208, 74-2088, 74-2615
and 75-3061.

United States Court of Appeals,
Ninth Circuit

May 27, 1976.

Rehearing Denied June 28, 1976.

A debtor corporation was adjudicated bankrupt, and appealed. Appeals were taken also from the denial of post-judgment motions by the United States District Court for the Southern District of California, Howard B. Turrentine, J. The Court of Appeals, Wollenberg, District Judge, sitting by designation, held that there was no error in reference to a special master, and the debtor received a fair and proper trial on the question of insolvency, with the use of a proper standard of what constitutes insolvency. The debtor's challenge to a Texas judgment was brought in the wrong forum. Where the debtor could not properly have attacked such a judgment collaterally, a motion to take a deposition for such purpose was properly denied.

Judgment in one case and order in another affirmed; other appeals dismissed; certain appeals treated as motions to remand, and denied.

1. Bankruptcy 60

Debtor's filing petition in California state court for judicial supervision of dissolution amounted to having procured, permitted or suffered "appointment of a receiver or trustee" within Bankruptcy Act, where effect of debtor's actions was to require its board of directors, under court supervision, to act as trustees: there was no need for board of directors to be formally appointed trustees or to formally possess legal title to corporation's assets. Bankr. Act, § 3, sub. a(5), 11 U.S.C.A. § 21(a)(5); West's Ann. Cal.Corp.Code, §§ 811, 4605, 4607-4611, 4614, 4616, 4617, 4800, 4801, 5000; West's Ann.Code Civ.Proc. §§ 564, 565.

See publication Words and Phrases for other judicial constructions and definitions.

2. Bankruptcy 65

Where debtor is insolvent or unable to pay his debts as they mature, he cannot defeat operation of bankruptcy laws by applying for dissolution under California law. Bankr.Act, § 3, sub. a(5), 11 U.S.C.A. § 21(a)(5); West's Ann.Cal.Corp.Code, §§ 811, 4605, 4607-4611, 4614, 4617, 4800, 4801, 5000; West's Ann.Code Civ.Proc. §§ 564, 565.

3. Bankruptcy 76(1)

Under Bankruptcy Act, intervening creditors took on status of petitioning creditors. Bankr.Act, § 59, sub. f, 11 U.S.C.A. § 95(f).

4. Bankruptcy 76(1)

Where part of judgment provided that property owned by debtor would be sold and proceeds of sale applied to reduce debtor's debt, and dispute arose over manner in which properties were to be appraised prior to sale, this was essentially dispute over manner in which judgment would be satisfied, and could not obscure fact that debtor's liability had already been fixed,

as against contention that claim was contingent as to liability and that creditor therefore had no status to petition for debtor's bankruptcy. Bankr.Act, § 59, sub. b, 11 U.S.C.A. § 95(b).

5. Bankruptcy 76(1)

Where debtor was in default on monthly payments, creditor's claim was not contingent as to liability; it was not necessary that creditor obtain judgment or accelerate due date of balance in order to achieve status of petitioning creditor under Bankruptcy Act. Bankr.Act, § 59, sub. b, 11 U.S.C.A. § 95(b).

6. Bankruptcy 76(1)

Where creditor held promissory note which had fully matured, creditor's claim was not contingent as to liability, for bankruptcy purposes, though there was dispute over indebtedness on another separate obligation to same creditor. Bankr.Act § 59, sub. b, 11 U.S.C.A. § 95(b).

7. Bankruptcy 93

Where debtor did not dispute that it had filed petition for judicial supervision of dissolution in state court but only disputed legal effect, debtor was not entitled to jury trial, in bankruptcy proceeding, on that issue. Bankr.Act, § 19, sub. a, 11 U.S.C.A. § 42(a).

8. Bankruptcy 94

In view of debtor's tangled financial affairs and duplication of those problems in two subsidiary corporations that had been merged into debtor three days before debtor's filing petition in state court for judicial supervision of dissolution, there was no abuse of discretion in reference to special master. Fed.Rules Civ.Proc. rule 53(b), 28 U.S.C.A.; Bankr.Act, § 19, sub. a, 11 U.S.C.A. § 42(a); Bankruptcy Gen. Order 37, 28 U.S.C.A.; Bankruptcy Rules, rule 513, 28 U.S.C.A.

9. Bankruptcy 94

Whether there was to be reference to special master was matter for district judge's determination in light of his perception of whether jury would find issue complicated, and debtor's request to examine special master on complexity of bankruptcy case was properly denied. Fed.Rules Civ.Proc. rule 53(b), 28 U.S.C.A.; Bankr.Act, § 19, sub. a, 11 U.S.C.A. § 42(a).

10. Bankruptcy 95

In providing that findings of special master are admissible as evidence and may be read to jury, rule did not require special master to personally read findings to jury, and it was not necessary that special master in bankruptcy case be made available for cross-examination on procedures used to reach findings presented to jury. Fed.Rules Civ.Proc. rule 53(e)(3), 28 U.S.C.A.; Bankr. Act, § 19, sub. a, 11 U.S.C.A. § 42(a).

11. Bankruptcy 94

Debtor in bankruptcy case was not prejudiced by fact that special master happened to be federal bankruptcy referee. Fed. Rules Civ.Proc. rule 53(b)(e)(3), 28 U.S.C.A.; Bankr.Act § 19, sub. a, 11 U.S.C.A. § 42(a).

12. Bankruptcy 93

Debtor's statutory right to jury trial under Bankruptcy Act gave it no greater rights than those available in civil proceedings governed by Seventh Amendment, and procedures employed by trial court, in making reference to special master and in allowing findings of special master to be read to jury, did not impermissibly interfere with Seventh Amendment right to jury trial. Fed.Rules Civ.Proc. rule 53(e)(3), 28 U.S.C.A.; Bankr.Act, § 19, sub. a, 11 U.S.C.A. § 42(a); U.S.C.A.Const. Amend. 7.

13. Bankruptcy 95

Under circumstances of case, including expert qualifications of special master, debtors' full opportunity to introduce evidence which would contradict special master's findings and to argue to jury that findings were incorrect and instructions given to jury on role of special master and weight to be given to his report, debtor received fair and proper trial on question of insolvency. Fed.Rules Civ.Proc. rule 53(e)(3), 28 U.S.C.A.; Bankr.Act, § 19, sub. a, 11 U.S.C.A. § 42(a); U.S.C.A.Const. Amend. 7.

14. Bankruptcy 95

In bankruptcy proceeding, trial judge properly instructed jury by giving "equity" definition of insolvency, following language of statute, and creditor, to show that debtor was "unable to pay debts as they mature" at time of petition for judicially supervised dissolution in state court was not obliged to show debtor's inability to pay "substantially" all of its debts rather than inability to pay one or two or three debts. Bankr. Act, § 3, sub. a(5), 11 U.S.C.A. § 21a(5).

See publication Words and Phrases for other judicial constructions and definitions.

15. Bankruptcy 462

Where appeal from bankruptcy judgment was pending, district court had no jurisdiction to enter order under rule authorizing relief from judgments or orders but rather could at most indicate that it would "entertain" such motion or indicate that it would grant such motion; in such event, debtor's next step would have been to apply to Court of Appeals for remand. Fed. Rules Civ.Proc. rule 60(b), 28 U.S.C.A.

16. Courts 405(12.16), 406.9(2)

District court's ruling that it was inappropriate to either grant or entertain motion for relief from judgment or order was only procedural ruling and not final determination of merits, and

thus was not appealable; "appeal" from such order was therefore considered as motion for remand of case for consideration of the motion. Fed.Rules Civ.Proc. rule 60(b), 28 U.S.C.A.

17. Federal Civil Procedure 2654

Where bank was not party to bankruptcy proceeding, its actions could not, absent evidence that any of the petitioning creditors knew of any possible irregularities, be charged to any adverse party in the bankruptcy proceeding, and alleged fraud was not a ground for relief from judgment in the bankruptcy proceeding. Fed.Rules Civ.Proc. rule 60(b), 28 U.S.C.A.

18. Judgment 472

Creditors petitioning for bankruptcy were entitled to rely on presumptive validity of judgment of United States District Court in Texas, absent challenge to its jurisdiction, and debtor's postjudgment collateral attack, in bankruptcy proceeding in United States District Court for.Southern District of California, upon the Texas judgment was brought in the wrong forum, even if it was too late to challenge judgment in the right forum. Fed. Rules Civ.Proc. rule 60(b), 28 U.S.C.A.

19. Federal Civil Procedure 2658

Where all pertinent information that was basis for motion for relief from judgment order should have been known to debtor well before trial on issue of its insolvency, debtor was not entitled to relief from judgment at time of such trial. Fed. Rules Civ.Proc. rule 60(b), 28 U.S.C.A.

20. Federal Civil Procedure 2655

Attempt to reargue primary appeal is not proper function of motion for relief from judgment or order. Fed.Rules Civ. Proc. rule 60(b), 28 U.S.C.A.

21. Courts 405(3.8)

Denial of request for permission to depose witness while appeal from adjudication was pending was appealable order. Fed.Rules Civ.Proc. rule 27(b), 28 U.S.C.A.

22. Federal Civil Procedure 1332

Where movant could not properly have collaterally attacked judgment, motion to take deposition for such purpose was properly denied. Fed.Rules Civ.Proc. rule 27(b), 28 U.S.C.A.

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OPINION

Before KOELSCH and GOODWIN, Circuit Judges, and WOLLENBERG,* District Judge.

WOLLENBERG, District Judge:

Crateo, Inc. a California corporation, was in the business of purchasing "sick" companies. Its own health came into question in late summer of 1970, and its creditors initiated involuntary bankruptcy proceedings. After a jury trial on the question of its ability to pay its debts, Crateo was adjudicated a bankrupt. While appeal from that judgment was pending, Crateo requested permission from the trial court to take depositions pursuant to Rule 27(b) of the Federal Rules of Civil Procedure. While its original appeal was still pending, Crateo also filed in the trial court two motions to vacate the adjudication of bankruptcy under Rule 60(b) of the Federal Rules of Civil Procedure. Appeals

* Honorable Albert C. Wollenberg, United States District Judge, Northern District of California, sitting by designation.

from the denial of all three post-judgment motions were consolidated with the primary appeal.[1] Finding no merit in any of appellant's arguments, we affirm the adjudication of bankruptcy and decline to remand the case for any further proceedings.

I. *Adjudication of Bankruptcy*

In the summer of 1970, Crateo elected to wind up its affairs and voluntarily dissolve. On August 31, 1970, it filed a petition for judicial supervision of the winding up process with the Superior Court of the State of California for San Diego County. See California Corporations Code § 4607. On that same day, the Superior Court ordered that notice of the dissolution proceeding be published and that all known creditors of Crateo be informed of the petition. In addition, the Superior Court ordered all creditor actions against Crateo enjoined and required all claims against Crateo to be presented in the dissolution proceedings. See California Corporations Code §§ 4608, 4616. Shortly thereafter, a creditors' petition was filed in the District Court alleging that Crateo had committed the fifth act of bankruptcy as defined by Section 3(a)(5) of the Bankruptcy Act, 11 U.S.C. § 21(a)(5).

In accord with Section 19(a) of the Bankruptcy Act, 11 U.S.C. § 42(a), Crateo requested a jury trial on the question of its insolvency. Prior to that trial, several issues, including the issue of Crateo's insolvency, were referred to the referee in bankruptcy sitting as a special master. The special master's report on the issue of Crateo's insolvency was read to the jury at trial. The jury subsequently found that Crateo was insolvent at the time it filed its petition for dissolution in the state court, and a judgment adjudicating Crateo a bankrupt was entered on August 9, 1973.

1. The appeal from the adjudication of bankruptcy is No. 73-3208. The appeal from the denial of permission to take post-judgment depositions is No. 74-2088. The appeals from the denials of the motions to vacate judgment are Nos. 74-2615 and 75-3061.

Appointment of a Receiver or Trustee

[1] The petitioning creditors alleged that Crateo's petition in the state court for judicial supervision of its dissolution amounted to the fifth act of bankruptcy, 11 U.S.C. § 21(a)(5). That section provides, in pertinent part, that:

> Acts of bankruptcy by a person shall consist of his having . . . (5) while insolvent or unable to pay his debts as they mature, procured, permitted, or suffered voluntarily or involuntarily the appointment of a receiver or trustee to take charge of his property.[2]

California law governing the dissolution of corporations creates a significant change in the status of the corporation and its directors. We agree with appellant's creditors and the District Court that the net effect of this change means that Crateo's actions in the state court resulted in the "appointment of a receiver or trustee" within the meaning of 11 U.S.C. § 21(a)(5).

After a petition for dissolution is filed, the board of directors continues to operate the corporation in order to settle its affairs. Cal.Corp.Code § 4800. However, directors may be removed by the superior court for reasons of "dishonesty, misconduct, neglect, or abuse of trust." Cal.Corp.Code § 4614. The court can take such an action on its own initiative, and the normal prerequisite of a shareholder's suit is not required. *Cf.* Cal.Corp. Code § 811.

The duties of the board of directors are also limited once the dissolution proceedings come under judicial supervision. The only business the corporation can carry on is that of winding up. Cal.Corp.Code § 4605. In carrying out this task, the board of directors is invested with extensive powers. Cal.Corp.Code § 4801. The powers of the board of directors, however, are not unlimited. The state court has the specific power to determine

2. The definition of "persons" in 11 U.S.C. § 1(23) makes this section applicable to corporations.

the manner in which claims are to be presented and settled and how shareholders' rights are to be determined. The court has the power to oversee the complete dissolution process and discharge the directors from their obligations after the process is completed. Cal.Corp.Code §§ 4608–11, 4617. In addition, the court has the general power to "make orders and adjudge as to any and all matters concerning the winding up of the affairs of the corporation." Cal.Corp.Code § 4607.

In winding up the corporation's affairs, the first duty of the board of directors is to satisfy the corporation's debts and liabilities. Cal.Corp.Code § 5000. In satisfying these obligations, the directors' powers under Cal.Corp.Code § 4801 are circumscribed by the overall supervisory power of the Superior Court under Cal.Corp.Code § 4607. If the directors do not settle the corporation's obligations properly, the court has the duty to vacate the directors' actions and make the appropriate settlement itself. *In re Trinity Tractor Co.*, 3 Cal.App.3d 428, 440-441, 83 Cal. Rptr. 783, 791–792 (1970).

In addition, Crateo's creditors could no longer pursue their normal legal remedies against Crateo once the Superior Court accepted Crateo's petition for judicial supervision of its dissolution proceedings. Actions already begun were stayed by the Superior Court's order. Whether or not legal title to the corporation's assets passed into the possession of the board of directors became irrelevant because creditors could sue neither entity.

There was no need for the board of directors to be formally appointed trustees or to formally possess legal title to the corporation's assets. The effect of Crateo's actions in the Superior Court was to require its board of directors, under court supervision, to act as trustees.[3] In determining whether a corporate

3. This result is not changed by the additional possibility that a receiver may be appointed pursuant to California Code of Civil Procedure §§ 564, 565.

dissolution under state law is the equivalent of the fifth act of bankruptcy, "it is the end result that counts." *In re Bonnie Classics*, 116 F.Supp. 646, 648 (S.D.N.Y.1953).[4]

[2] Not every corporate petition for dissolution under the California Corporations Code will necessarily result in an involuntary bankruptcy. Under 11 U.S.C. § 21(a)(5), the creditors must also show that the debtor was "insolvent or unable to pay his debts as they mature." However, if this situation exists, California corporations cannot defeat the operation of the bankruptcy laws by applying for dissolution under California law. *In re Watts & Sachs*, 190 U.S. 1, 27, 23 S.Ct. 718, 47 L.Ed. 933 (1902). The overly technical approach to the interpretation of 11 U.S.C. § 21(a)(5) urged by Crateo must be rejected.

Petitioning Creditors

[3] The creditors' petition against Crateo was required by Section 59(b) of the Bankruptcy Act, 11 U.S.C. § 95(b), to be filed by at least "three or more creditors who have provable

4. *Blair & Co., Inc. v. Foley*, 471 F.2d 178 (2d Cir. 1972), *vacated and remanded for consideration of mootness*, 414 U.S. 212, 94 S.Ct. 405, 38 L.Ed.2d 422 (1973), is not to the contrary. That case involved a private arrangement between a brokerage firm and the New York Stock Exchange for the appointment of a liquidating agent for the firm. No court was involved in the liquidation process nor did the winding up process force creditors to forego their normal legal remedies. In light of the different factual situation herein, we need not comment further on the *Blair* case.

claims not contingent as to liability." Six petitioning creditors[5] presented evidence before the special master, and Crateo claims that none of them had claims "not contingent as to liability." Examination of the creditors' claims, however, shows that appellant is incorrect.

[4] Intermark Investing Inc. was a judgment creditor of Crateo's pursuant to a stipulated judgment entered in a state court prior to the filing of the creditors' petition. Part of the judgment provided that two parcels of property owned by Crateo would be sold and the proceeds of the sale applied to reduce Crateo's debt to Intermark. A dispute arose over the manner in which the properties were to be appraised prior to their sale. This was essentially a dispute over the manner in which the judgment would be satisfied and cannot obscure the fact that Crateo's liability to Intermark had already been fixed. *In re Trimble Co.*, 339 F.2d 838, 844 (3rd Cir. 1964).

[5] Under a promissory note to Olympia Business Service, Inc., Crateo was obligated to pay $1200 per month. Since appellant did not make the payments due July 1, 1970, and August 1, 1970, Olympia was properly determined to be a creditor whose claim was not contingent as to liability. There was no need for Olympia to obtain a judgment against Crateo before it could achieve the status of a petitioning creditor under Section 59(b). *Denham v. Shellman Grain Elevator, Inc.*, 444 F.2d 1376, 1380 (5th Cir. 1971). Whether or not Crateo received proper notice so as to accelerate payment of the entire amount remaining on the promissory note is irrelevant because the two monthly installments were definitely due at the time the creditors' petition was filed.

5. Two of the original petitioning creditors and four intervening creditors presented evidence before the special master on this question. Under 11 U.S.C. § 95(f), the intervening creditors took on the status of petitioning creditors. *3 Collier on Bankruptcy* ¶ 59.29 (14th ed. 1975).

[6] General Electric Company held two promissory notes which had fully matured prior to August 31, 1970. Again, there was no need for General Electric to have obtained judgments on these notes in order to satisfy the requirements of Section 59(b). The fact that there was a dispute over Crateo's indebtedness on another separate obligation to General Electric is irrelevant.[6]

Use of Special Master's Report at Jury Trial

[7] Under Section 19(a) of the Bankruptcy Act, 11 U.S.C. § 42(a), Crateo was entitled to a jury trial "in respect to the question of [its] insolvency."[7] Prior to that trial, the issue of Crateo's insolvency had been referred to the referee in bankruptcy sitting as a special master. The report of the special master was then read to the jury pursuant to Rule 53(e)(3) of the Federal Rules of Civil Procedure. Crateo contends that the procedure followed in this case violated its right to a trial by jury on the question of its insolvency.

[8,9] Crateo first claims that reference to a special master was unwarranted because the issues were readily understandable by a jury. F.R.C.P. Rule 53(b) provides that "in actions to be tried to a jury, a reference shall be made only when the issues

6. While it would not be helpful to discuss the claims of the three other petitioning creditors, we believe the District Court correctly held that their claims were not contingent as to liability.

7. Although 11 U.S.C. § 42(a) also gives debtors the right to a jury trial on the question of whether they committed an act of bankruptcy, there was no need for a jury trial on that issue in this case. Crateo did not dispute the fact that it had filed a petition for judicial supervision of dissolution in the state court. Crateo only disputed the legal effect that would be attached to its action.

are complicated."[8] The petitioning creditors had alleged that Crateo was bankrupt because it could not pay its debts as they matured. While every claim of this type does not require use of a master, considering Crateo's tangled financial affairs and the duplication of those problems in two subsidiary corporations that had been merged into Crateo three days before the filing of the petition in state court for judicial supervision of dissolution, we believe that there was no abuse of discretion in reference to the special master. Since this was a matter for the district judge's determination in light of his perception of whether the jury would find the issue complicated, Crateo's request to examine the special master on the complexity of the case was properly denied.

[10] At the trial, the findings of the special master were read to the jury. In providing that these findings are "admissible as evidence" and "may be read to the jury," Rule 53(e)(3) does not require the special master to personally read the findings to the jury. Consequently, contrary to appellant's position, the special master did not have to be made available for cross examination on the procedures used to reach the findings presented to the jury.

[11-13] The expert qualifications of the special master were Crateo's primary guarantee that the proper legal standards and procedures were used by the master in determining his findings.

8. The trial was held in June of 1973. General Order in Bankruptcy No. 37 was in effect at that time and made Rule 53 of the Federal Rules of Civil Procedure applicable to jury trials in bankruptcy cases. *Cf. Diamond Door Co. v. Lane-Stanton Lumber Co.*, 505 F.2d 1199 (9th Cir. 1974). The Federal Rules of Civil Procedure with respect to masters now apply to bankruptcy proceedings because of Bankruptcy Rule 513.

In this respect, it is significant that Crateo did not object to the qualifications of the master appointed in this case.[9] At the trial, Crateo was given a full opportunity to introduce evidence that would contradict the findings of the special master and argue to the jury that the findings were incorrect. The jury was instructed on the role of the special master and the weight to be given to his report, and Crateo did not object to this instruction.

The procedures employed in the trial would not impermissibly interfere with the right to trial by jury guaranteed by the Seventh Amendment. *Ex parte Peterson*, 253 U.S. 300, 40 S.Ct. 543, 64 L.Ed. 919 (1920); *Burgess v. Williams*, 302 F.2d 91 (4th Cir. 1962). Crateo's statutory right to a jury trial under the Bankruptcy Act gives it no greater rights than those available in civil proceedings governed by the Seventh Amendment. *Diamond Door Co. v. Lane-Stanton Lumber Co.*, 505 F.2d 1199 (9th Cir. 1974). Under all the circumstances of this case, we conclude that Crateo received a fair and proper trial on the question of its insolvency.

Jury Instructions

[14] The petitioning creditors had alleged and were required to prove that Crateo was "unable to pay [its] debts as they mature" when it petitioned for a judicially supervised dissolution in state court. 11 U.S.C. § 21(a)(5). This is the "equity" definition of insolvency. The trial judge's instruction to the jury followed the language of the statute.[10] Crateo objected to this

9. Crateo was not prejudiced by the fact that the special master happened to be a federal bankruptcy referee.

10. The jury was instructed that "considering only those items which you have concluded are both debts and are mature, you must decide whether Crateo, Inc. had the ability to pay these debts on August 31, 1970."

instruction, claiming that the word "debts" is in the plural and therefore the creditor must show the debtor's inability to pay "substantially all" of its debts and not just the debtor's inability to pay "one or two or three" debts.

The words "unable to pay [its] debts as they mature" are contained in a statutory context which necessitates rejection of Crateo's argument. A debtor commits the fifth act of bankruptcy when he is unable to pay his debts as they mature *and* a receiver or trustee is appointed to take charge of his property.[11] In that situation, there is a good possibility that some creditors may not be able to recover their claims on an equitable basis with other creditors unless they are able to invoke the protections of the Bankruptcy Act. Without those protections, the fact that some, or even most, of the creditors could be paid is of little consolation to those who cannot be paid. Adoption of Crateo's position would be completely contrary to the increasing amount of protection afforded to creditors by successive revisions of 11 U.S.C. § 21(a)(5).[12] In addition, Crateo's proposed test would be so indefinite as to be unworkable. The trial judge properly declined to modify his instructions.

II. *Motions to Vacate the Adjudication of Bankruptcy*

[15] Approximately eight months after judgment was entered adjudicating Crateo to be a bankrupt, and while the appeal from the judgment was pending, Crateo filed a motion

11. Thus, contrary to the implications in Crateo's argument, debtors are not thrown into bankruptcy merely because they cannot pay a few small debts at a particular moment.

12. See *1 Collier on Bankruptcy* ¶ 3.501 (14th ed. 1974).

in the District Court to vacate the judgment under Rule 60(b) of the Federal Rules of Civil Procedure. Because of the pending appeal, the District Court had no jurisdiction to enter an order under Rule 60(b). The most the District Court could do was to either indicate that it would "entertain" such a motion or indicate that it would grant such a motion. If appellant had received such an indication, its next step would have been to apply to this Court for a remand. *Canadian Ingersoll-Rand Co. v. Peterson Products*, 350 F.2d 18, 27–28 (9th Cir. 1965).

[16] In this case, however, the District Court found that it was inappropriate to either grant or entertain the Rule 60(b) motion. This was only a procedural ruling and not a final determination of the merits of the Rule 60(b) motion. Such an order is not appealable. Crateo's "appeal" from the District Court's order must therefore be considered as a motion for remand of the case for consideration of the Rule 60(b) motion. *Weiss v. Hunna*, 312 F.2d 711, 713 (2d Cir. 1963) *cert. denied*, 374 U.S. 753, 83 S.Ct. 1920, 10 L.Ed.2d 1073 (1963); *Canadian Ingersoll-Rand Co. v. Peterson Products, supra*, 350 F.2d at 27 n. 16. We decline to order such a remand.

The basis of Crateo's motion was an attack upon the validity of a judgment from the United States District Court for the Southern District of Texas in favor of the Southern National Bank of Houston and against Crateo. See *Southern National Bank of Houston v. Tri Financial Corporation*, 317 F.Supp. 1173 (S.D.Tex.1970), *affirmed sub nom., Southern National Bank of Houston v. Crateo, Inc.*, 458 F.2d 688 (5th Cir. 1972). This judgment was introduced as evidence tending to prove that Crateo was unable to pay its debts as they matured and comprised a large proportion of Crateo's unpaid debts. In its Rule 60(b) motion, Crateo claimed that the Texas judgment was obtained by fraud and should not have been considered at Crateo's bankruptcy trial.

The District Court in Texas had determined that Tri Financial, a predecessor of Crateo, was obligated to purchase a promissory note from the bank. While that decision was on appeal to the Fifth Circuit, the bank brought an action against one of the signers of the note in the United States District Court for the District of Nevada. After the defendant in the Nevada action raised the claim that her signature on the note had been forged, the bank decided not to prosecute its suit and the case was dismissed. The Fifth Circuit's decision came after the events in Nevada.

[17] The bank, however, was not a party in Crateo's bankruptcy proceeding. The Texas judgment was merely introduced into evidence by other creditors of Crateo as tending to show Crateo was unable to pay its debts as they matured. There is no indication that any of those petitioning creditors knew of any possible irregularities connected with the evidence. Despite Crateo's protestations of fraud in the obtaining of the Texas judgment, its Rule 60(b) motion in this case cannot be considered as falling under the third clause of that section because the bank's actions cannot be charged to any adverse party in the bankruptcy proceeding.[13]

[18] The jurisdiction of the District Court in Texas over the parties in *Southern National Bank of Houston v. Tri Financial Corporation, supra,* was not challenged in the bankruptcy proceedings, and the petitioning creditors were entitled to rely on

13. Assuming that the inability to collect from one of the alleged signers of the promissory note eliminated Tri Financial's obligation to purchase the note from the bank, any possible fraudulent conduct in this situation would consist of the bank not informing the Fifth Circuit of the invalidity of the obligation before it affirmed the judgment of the District Court in Texas.

the judgment's presumptive validity. Crateo's post-judgment collateral attack on the Texas judgment was brought in the wrong forum.[14]

In its Rule 60(b) motion, Crateo also claimed that the bank had received some payments on the promissory note and that Crateo's indebtedness to the bank was therefore less than the amount stated in the Texas judgment. Again, the collateral attack on a presumptively valid judgment was brought in the wrong forum.

[19, 20] We also decline to remand the case because of Crateo's second Rule 60(b) motion. All of the pertinent information that is the basis for this motion should have been known to Crateo well before the 1973 trial on the issue of its insolvency. There is no excuse for waiting over two years after entry of judgment before filing this motion.[15]

III. *Perpetuation of Testimony Pending Appeal*

[21] While the appeal from the adjudication of bankruptcy was pending, Crateo requested permission, pursuant to Rule 27(b)

14. The bank's Nevada action terminated in June of 1971, and the trial on the issue of Crateo's insolvency did not take place until June of 1973. Crateo first raised this issue in early 1974 when it moved for an order perpetuating testimony pending appeal. No satisfactory explanation of the delay in producing evidence of the Nevada action is provided. The possibility that it may have been too late to petition either the Fifth Circuit or the District Court in Texas to set aside their judgments does not allow Crateo to collaterally attack the judgment in this proceeding.

15. Many of the arguments raised by Crateo with respect to these two Rule 60(b) motions are irrelevant to the motions and are attempts to reargue the primary appeal. This is not the proper function of a Rule 60(b) motion.

of the Federal Rules of Civil Procedure, to depose an officer of the Southern National Bank of Houston. This testimony was allegedly needed to investigate the circumstances surrounding the purported forgery on the promissory note and the satisfaction of the note discussed in part II, *supra*. The order denying Crateo's motion is an appealable order. *Ash v. Cort*, 512 F.2d 909 (3rd Cir. 1975). *Cf. Martin v. Reynolds Metals Corporation*, 297 F.2d 49 (9th Cir. 1961).

[22] On appeal, we must decide whether there was an abuse of discretion by the trial court. *Ash v. Cort, supra.* For the reasons stated previously in part II, *supra*, Crateo could not collaterally attack the Texas judgment. There was, therefore, no reason in this bankruptcy proceeding to take depositions on the subject. Crateo's motion was properly denied.

The judgment in No. 73-3208 and the order in No. 74-2088 are affirmed. The appeals in Nos. 74-2615 and 75-3061 are dismissed. Considering Nos. 74-2615 and 75-3061 as motions to remand to permit the district judge to consider appellant's Rule 60(b) motions, the motions are denied.

STATUTES AND RULES

California Corporations Code

§811. Removal of Directors by Superior Court. The superior court of the county where the principal office is located may, at the suit of shareholders holding at least 10 percent of the number of outstanding shares with or without voting rights, remove from office any director in case of fraudulent or dishonest acts or gross abuse of authority or discretion with reference to the corporation, and may bar from reelection any director so removed for a period prescribed by the court. The corporation shall be made a party to such actions.

§4605. Cessation of Business -- Notice of Commencement of Proceedings. When a voluntary proceeding for winding up has commenced, the corporation shall cease to carry on business except to the extent necessary for the beneficial winding up thereof, and except during such period as the board of directors may deem necessary to preserve the corporation's good will or going-concern value pending a sale of its business or assets, or both, in whole or in part. The directors forthwith shall cause written notice of the commencement of the proceeding for voluntary winding up to be given by mail to all shareholders and to all known creditors and claimants whose addresses appear on the records of the corporation.

§4606. Revocation of Authorization to Wind Up -- Certificate of Revocation -- Execution, Filing and Contents. A voluntary election to wind up and dissolve may be revoked prior to distribution of any assets by the vote or written consent of shareholders or members representing no less than a majority of the voting power, or by resolution of the board of directors if the election was by the directors pursuant to Section 4601. Thereupon a certificate evidencing the revocation shall be subscribed, verified and filed in the manner prescribed by Section 4603.

The certificate shall set forth:

(a) That the corporation has revoked its election to wind up and dissolve.

(b) That no assets have been distributed pursuant to the election.

(c) If the revocation was made by the vote or written consent of shareholders or members, the number of shares or memberships voting for or consenting to the revocation and the total number of outstanding shares or memberships the holders of which were entitled to vote on or consent to the revocation.

(d) If the election and revocation was by resolution of the board of directors it shall be so stated.

§4607. Court Supervision of Voluntary Winding Up -- Protection of Rights of Home Purchases. If a corporation is in the process of voluntary winding up, the superior court of the county in which the principal office of the corporation is located, upon the petition of (a) the corporation, or (b) the holders of 5 percent or more of the number of its outstanding shares, or of (c) three or more creditors, or of (d) three or more persons who have purchased homes from a construction corporation, and upon such notice to the corporation and to other persons interested in the corporation as shareholders or creditors as the court may order, may make orders and adjudge as to any and all matters concerning the winding up of the affairs of the corporation.

If the corporation has, within 18 months prior to the commencement of the proceedings for winding up, been engaged in the business of constructing, or contracting or subcontracting for the construction of buildings for residential use, the court shall, in making orders and adjudging as to matters concerning the winding up, make such provision as it deems reasonably necessary to protect the rights of the purchasers of the homes, including rights which may arise against the corporation for

breach of warranties in connection with the construction. The protection so afforded shall extend to rights which may arise with respect to buildings whose construction was completed within 18 months prior to the commencement of the proceedings for winding up, and the orders and decrees extending the protections shall have a duration of at least 18 months after the filing of the petition but may be made effective for a longer period at the discretion of the court.

§4608. Presentation and Proof of Claims in Court Proceedings -- Notice to Creditors. The jurisdiction of the court includes the presentation and proof of all claims and demands against the corporation, whether due or not yet due, contingent, unliquidated, or sounding only in damages, and the barring from participation of creditors and claimants failing to make and present claims and proofs as required by any order.

All creditors and claimants may be barred from participation in any distribution of the general assets if they fail to make and present claims and proofs within such time as the court may direct, which shall not be less than four nor more than six months after the first publication of notice to creditors unless it appears by affidavit that there are no claims, in which case the time limited may be three months. If it is shown that a claimant did not receive notice because of absence from the State or other cause, the court may allow a claim to be filed or presented at any time before distribution is completed.

Such notice to creditors shall be published not less than once a week for three consecutive weeks in some newspaper of general circulation published in the county in which the principal office is located, or, if there is no such newspaper published in that county, in such newspaper as may be designated by the court, directing creditors and claimants to make and present claims and proofs to the person, at the place, and within the time limited by the order. A copy of the notice shall be mailed to each person shown as a creditor or claimant by the books of the corporation, at his last known address.

Holders of secured claims may prove for the whole debt in order to realize any deficiency. If such creditors fail to present their claims they shall be barred only as to any right to claim against the general assets for any deficiency in the amount realized on their security.

Before any distribution is made the amount of any unmatured, contingent, or disputed claim against the corporation which has been presented and has not been disallowed, or such part of any such claim as the holder would be entitled to if the claim were due, established, or absolute, shall be paid into court and there remain to be paid over to the party when he becomes entitled thereto, or if he fails to establish his claim, to be paid over or distributed with the other assets of the corporation to those entitled thereto, or such other provision for the payment of such claim shall be made as the court may deem adequate. If a creditor whose claim has been allowed but is not yet due consents to the payment of the present value of his claim he shall be entitled to its present value upon distribution.

Suits against the corporation on claims which have been rejected shall be commenced within 30 days after written notice of rejection thereof is given to the claimant.

§4609. Settlement of Claims in Court Proceeding. The jurisdiction of the court includes the settlement or determination of all claims of every nature against the corporation or any of its property, or the amount of money or assets required to be retained to pay or provide for the payment of such claims, or any claim, or the amount of money or assets available for distribution among shareholders from time to time. The court may order the bringing in of new parties as it deems proper for the determination of all questions and matters.

§4610. Judicial Determination of Rights of Shareholders to Assets. The jurisdiction of the court includes the determination of the rights of shareholders and of all classes of shareholders in and to the assets of the corporation.

§4611. Judicial Determination of Accounts of Directors. The jurisdiction of the court includes the presentation and the filing of intermediate and final accounts of the directors and hearings thereon, and the allowance, disallowance, or settlement thereof, and the discharge of the directors from their duties and liabilities.

§4800. Function of Directors in Voluntary Proceedings. When voluntary proceedings for winding up or dissolution of a corporation have been commenced, the board of directors shall continue to act as a board and shall have full powers to wind up and settle its affairs. If the directors have not theretofore elected officers of the corporation pursuant to Section 821, the directors shall elect them and such assistants as the directors deem proper. Any act authorized or approved by a majority of the directors acting as a board is valid and binding as though authorized and consented to by all of the directors.

§5000. Distribution of Assets to Shareholders. After determining that all the known debts and liabilities of a corporation in the process of winding up have been paid or adequately provided for, the directors shall distribute all the remaining corporate assets among the shareholders and owners of shares according to their respective rights and preferences. If the winding up is by court proceeding or subject to court supervision, the distribution shall not be made until after the expiration of any period for the presentation of claims which has been prescribed by order of court.

Bankruptcy Act Provisions

§3(5), 11 U.S.C. §21a(5):

Acts of Bankruptcy

(a) Acts of bankruptcy by a person shall consist of his having . . . (5) while insolvent or unable to pay his debts as they mature, procured, permitted, or suffered voluntarily or

involuntarily the appointment of a receiver or trustee to take charge of his property . . .

§19(a), 11 U.S.C. §42a:

Jury Trials

(a) A person against whom an involuntary petition has been filed shall be entitled to have a trial by jury in respect to the question of his insolvency, except as herein otherwise provided, and of any act of bankruptcy alleged in such petition to have been committed, upon filing a written application therefor at or before the time within which an answer may be filed. If such application is not filed within such time, a trial by jury shall be deemed to have been waived.

§44, 11 U.S.C. §72:

Trustees; creditors' committees; and attorneys

(a) The creditors of a bankrupt, exclusive of the bankrupt's relatives or, where the bankrupt is a corporation, exclusive of its stockholders or members, its officers, and the members of its board of directors or trustees or of other similar controlling bodies, shall at the first meeting of creditors after the adjudication, or after a vacancy has occurred in the office of trustee, or after an estate has been reopened, appoint a trustee or three trustees of such estate. If the creditors do not appoint a trustee or if the trustee so appointed fails to qualify as herein provided, the court shall make the appointment. If the bankrupt is a face-amount certificate company, as defined in section 80a -- 4 of Title 15, the court alone shall make the appointment; but the court shall not make such appointment without first notifying the Securities and Exchange Commission and giving it an opportunity to be heard.

(b) Such creditors may, at their first meeting, also appoint a committee of not less than three creditors, which committee may consult and advise with the trustee in connection with the

administration of the estate, make recommendations to the trustee in the performance of his duties and submit to the court any question affecting the administration of the estate.

(c) An attorney shall not be disqualified to act as attorney for a receiver or trustee merely by reason of his representation of a general creditor. July 1, 1898, c. 541, § 44, 30 Stat. 557; June 22, 1938, c. 575, § 1, 52 Stat. 860; Aug. 22, 1940, c. 686, Title I, § 29(b), 54 Stat. 835.

§59(b), 11 U.S.C. 95b:

Who May File and Dismiss Petitions

. . . (b) Three or more creditors who have provable claims not contingent as to liability against a person, amounting in the aggregate to $500 in excess of the value of any securities held by them, or, if all of the creditors of the person are less than twelve in number, then one or more of the creditors whose claim or claims equal that amount, may file a petition to have him adjudged a bankrupt; but the claim or claims, if unliquidated, shall not be counted in computing the number and the aggregate amount of the claims of the creditors joining in the peition, if the court determines that the claim or claims cannot be readily determined or estimated to be sufficient, together with the claims of the other creditors, to aggregate $500, without unduly delaying the decision upon the adjudication.

§63(a), 11 U.S.C. §103a:

Debts Which May Be Proved

(a) Debts of the bankrupt may be proved and allowed against his estate which are founded upon . . .

F.R.C.P. 53:

Masters

(a) Appointment and Compensation. Each district court with the concurrence of a majority of all the judges thereof may

appoint one or more standing masters for its district, and the court in which any action is pending may appoint a special master therein. As used in these rules the word "master" includes a referree, an auditor, an examiner, a commissioner, and an assessor. The compensation to be allowed to a master shall be fixed by the court, and shall be charged upon such of the parties or paid out of any fund or subject matter of the action, which is in the custody and control of the court as the court may direct. The master shall not retain his report as security for his compensation; but when the party ordered to pay the compensation allowed by the court does not pay it after notice and within the time prescribed by the court, the master is entitled to a writ of execution against the delinquent party.

(b) Reference. A reference to a master shall be the exception and not the rule. In actions to be tried by a jury, a reference shall be made only when the issues are complicated; in actions to be tried without a jury, save in matters of account and of difficult computation of damages, a reference shall be made only upon a showing that some exceptional condition requires it.

(c) Powers. The order of reference to the master may specify or limit his powers and may direct him to report only upon particular issues or to do or perform particular acts or to receive and report evidence only and may fix the time and place for beginning and closing the hearings and for the filing of the master's report. Subject to the specifications and limitations stated in the order, the master has and shall exercise the power to regulate all proceedings in every hearing before him and to do all acts and take all measures necessary or proper for the efficient performance of his duties under the order. He may require the production before him of evidence upon all matters embraced in the reference, including the production of all books, papers, vouchers, documents, and writings applicable thereto. He may rule upon the admissibility of evidence unless otherwise directed by the order of reference and has the authority to put

witnesses on oath and may himself examine them and may call the parties to the action and examine them upon oath. When a party so requests, the master shall make a record of the evidence offered and excluded in the same manner and subject to the same limitations as provided in Rule 43(c) for a court sitting without jury.

(d) Proceedings.

(1) Meetings. When a reference is made, the clerk shall forthwith furnish the master with a copy of the order of reference. Upon receipt thereof unless the order of reference otherwise provides, the master shall forthwith set a time and place for the first meeting of the parties or their attorneys to be held within 20 days after the date of the order of reference and shall notify the parties or their attorneys. It is the duty of the master to proceed with all reasonable diligence. Either party, on notice to the parties and master, may apply to the court for an order requiring the master to speed the proceedings and to make his report. If a party fails to appear at the time and place appointed, the master may proceed ex parte or, in his discretion, adjourn the proceedings to a future day, giving notice to the absent party of the adjournment.

(2) Witnesses. The parties may procure the attendance of witnesses before the master by the issuance and service of subpoenas as provided in Rule 45. If without adequate excuse a witness fails to appear or give evidence, he may be punished as for a contempt and be subjected to the consequences, penalties, and remedies provided in Rules 37 and 45.

(3) Statement of Accounts. When matters of accounting are in issue before the master, he may prescribe the form in which the accounts shall be submitted and in any proper case may require or receive in evidence a statement by a certified public accountant who is called as a witness. Upon objection of a party to any of the items thus submitted or upon a showing that the form of statement is insufficient, the master may require

a different form of statement to be furnished, or the accounts or specific items thereof to be proved by oral examination of the accounting parties or upon written interrogatories or in such other manner as he directs.

(e) Report.

(1) Contents and Filing. The master shall prepare a report upon the matters submitted to him by the order of reference and, if required to make findings of fact and conclusions of law, he shall set them forth in the report. He shall file the report with the clerk of the court and in an action to be tried without a jury, unless otherwise directed by the order of reference, shall file with it a transcript of the proceedings and of the evidence and the original exhibits. The clerk shall forthwith mail to all parties notice of the filing.

(2) In Non-Jury Actions. In an action to be tried without a jury the court shall accept the master's findings of fact unless clearly erroneous. Within 10 days after being served with notice of the filing of the report any party may serve written objections thereto upon the other parties. Application to the court for action upon the report and upon objections thereto shall be by motion and upon notice as prescribed in Rule 6(d). The court after hearing may adopt the report or may modify it or may reject it in whole or in part or may receive further evidence or may recommit it with instructions.

(3) In Jury Actions. In an action to be tried by a jury the master shall not be directed to report the evidence. His findings upon the issues submitted to him are admissible as evidence of the matters found and may be read to the jury, subject to the ruling of the court upon any objections in point of law which may be made to the report.

(4) Stipulation as to Findings. The effect of a master's report is the same whether or not the parties have consented to the reference; but, when the parties stipulate that a master's findings of fact shall be final, only questions of law arising upon the report shall thereafter be considered.

(5) Draft Report. Before filing his report a master may submit a draft thereof to counsel for all parties for the purpose of receiving their suggestions.

AS amended Feb. 28, 1966, eff. July 1, 1966.

F.R.C.P. 60:

Relief from Judgment or Order

. . . (b) Mistakes; Inadvertence; Excusable Neglect; Newly Discovered Evidence; Fraud, etc. On motion and upon such terms as are just, the court may relieve a party or his legal representative from a final judgment, order, or proceeding for the following reasons: (1) mistake, inadvertence, surprise, or excusable neglect; (2) newly discovered evidence which by due diligence could not have been discovered in time to move for a new trial under Rule 59(b); (3) fraud (whether heretofore denominated intrinsic or extrinsic), misrepresentation, or other misconduct of an adverse party; (4) the judgment is void; (5) the judgment has been satisfied, released, or discharged, or a prior judgment upon which it is based has been reversed or otherwise vacated, or it is no longer equitable that the judgment should have prospective application; or (6) any other reason justifying relief from the operation of the judgment. The motion shall be made within a reasonable time, and for reasons (1), (2), and (3) not more than one year after the judgment, order, or proceeding was entered or taken. A motion under this subdivision (b) does not affect the finality of a judgment or suspend its operation. This rule does not limit the power of a court to entertain an independent action to relieve a party from a judgment, order, or proceeding, or to grant relief to a defendant not actually personally notified as provided in Title 28 U.S.C., § 1655, or to set aside a judgment for fraud upon the court. Writs of coram nobis, coram vobis, audita querela, and bills of review and bills in the nature of a bill of review, are abolished, and the procedure for obtaining any relief from a judgment shall be by motion as prescribed in these rules or by an independent action. As amended Dec. 27, 1946, eff. March 19, 1948; Dec. 29, 1948, eff. Oct. 20, 1949.

No. 76-226

In the Supreme Court of the United States

OCTOBER TERM, 1976

In Re CRATEO, INC.,

Bankrupt,

CRATEO, INC.,

Petitioner,

v.

INTERMARK, INC., et al.,

Respondent.

REBUTTAL BRIEF CALLING ATTENTION TO FACTUAL ERRORS IN RESPONDENTS' BRIEF

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TABLE OF AUTHORITIES

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REBUTTAL BRIEF CALLING ATTENTION TO FACTUAL ERRORS IN RESPONDENTS' BRIEF

Petitioner respectfully directs the Court's attention to four erroneous statements in the Opposition Brief of Respondents:

(1)

Respondents, on page 9 of their Brief, asserted that the portion of the decision of the Ninth Circuit which "imposed" duties upon directors and "deprived" shareholders of rights, was not raised below. That assertion is incorrect.

The Ninth Circuit in its opinion failed to discuss the serious constitutional issues which arise from converting directors

into trustees for creditors, such as (1) imposing fiduciary duties to creditors upon the directors without "due process"; (2) forcing directors into the involuntary servitude of creditors, (3) depriving shareholders of control of the corporation without "due process"; (4) denying creditors their statutory right to select a trustee as provided by Section 44 of the Bankruptcy Act; and (5) placing directors in civil jeopardy for violating State law.

Those matters were all extensively briefed to the Ninth Circuit as set forth in Item (1) of the Appendix.

(2)

Respondents, on page 12 of their Brief, dealing with the need for a disinterested receiver, stated that "Crateo did not raise this argument in the Courts below." That statement is incorrect.

The requirement of a disinterested receiver or trustee was extensively briefed to the Ninth Circuit as is set forth in Item (2) of the Appendix.

The point, of course, is that the Ninth Circuit did not discuss the requirement of a disinterested trustee, but by holding that Crateo's actions in the State Court resulted in the "appointment of a receiver or trustee" it, in effect, stated that Crateo's directors (notwithstanding that they were adverse to creditors) became trustees for creditors.

This places the Ninth Circuit in conflict with both California Statute and the Eighth Circuit on the need for a disinterested trustee.

(3)

Respondents stated relative to the fraudulent Texas judgment on page 13 of its Opposition Brief that "Crateo could not explain satisfactorily the reason for its delay of two and one-half years in raising the issue of the use of alleged extrinsic fraud in procuring the judgment."

The answer to that is that Crateo simply did not know of the fraud. As soon as it discovered the fraud it made motions to perpetrate testimony, and to set aside the judgment on grounds of newly discovered evidence. There was a time lag of only 12 days from the time of discovery of the fraud to the time of calling that discovery to the Court's attention, and a portion of that 12 days involved the Christmas holidays. You can't inform someone of a fraud until you first know about it.

This matter was presented in extensive fashion in two motions to the Trial Court and in two appeals to the Ninth Circuit. Please refer to Item (3) of the Appendix.

(4)

Petitioner pointed out it was not required to attack the Texas judgment in the Texas rendering Court, but, rather, that since the fraud of concealment was also committed in the Court below, that fraud could be attacked in the Court below.

Respondents, on page 13 of their Brief, incorrectly asserted this point was not raised below. In fact, it was extensively briefed before the Ninth Circuit. The Ninth Circuit itself devoted four paragraphs to this matter (pages A-12 to 13 of Petitioner's Petition). Item (4) of the Appendix recites portions of the Briefs below.

The point, of course, is that Respondents are attempting to profit from the fraud of another by utilizing that fraud to make up 40% of the claimed debt which Crateo was supposedly unable to pay as it matured.

CONCLUSION

Petitioner respectfully requests this Honorable Court to disregard the incorrect statements of Respondents and to grant Certiorari to resolve the multiple conflicts among the various circuits as set forth in its Petition.

Respectfully submitted,

WALTER WENCKE
Attorney for Petitioner

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Of Counsel

APPENDIX

(1)

The Serious Constitutional Problems Involved in Converting Directors into Trustees for Creditors were Briefed Below.

Crateo, in its "Apppellants Opening Brief" No. 74-2615, pages 31-34, specifically called the Court's attention to the following:

> "This Brief shows there are also constitutional problems affecting Directors, Shareholders and Creditors which will arise from the attempt to convert Directors into Trustees for Creditors by interpreting Section 3a(5) of the Bankruptcy Act to change the clear meaning of the California Corporations Code.
>
> "The California Statute specifically provides that Directors continue to act as Directors:
>
> > 'Where voluntary proceedings for Winding Up of Dissolution of a Corporation have been commenced, the *Board of Directors shall continue to act as a Board*. . . .' (Cal. Corp. Code Sec. 4800.)
>
> "Intermark and the other petitioning creditors argue that filing the voluntary proceedings for dissolution converted the directors into 'Receivers or Trustees for Creditors' by virtue of Section 3a(5) of the Bankruptcy Act.
>
> . . .

"In other words the federal code section was used by the creditors and the Court below to cast a totally different meaning upon a California Statute.

"This usage or interpretation of the federal statute 3a(5) would render that statute unconstitutional for the following reasons:

. . .

"(b) *Fiduciary duties to creditors would be imposed upon Directors without "due process."*

"Under Intermark's thesis Bankruptcy Section 3a(5) alters the California Corporations Code relative to Directors and the Directors owe a 'fiduciary duty' to the creditors forthwith upon filing the voluntary dissolution proceedings. Yet, clearly, the Directors accepted no such fiduciary duty to creditors. To interpret Section 3a(5) as foisting a 'fiduciary duty to creditors' upon the Directors contrary to the Directors' wishes and without notice and hearing, violates the 'due process' required by the 14th Amendment to the Constitution.

"(c) *The obligation of contract between the Directors and Shareholders would be impaired.*

"The Intermark thesis of using 3a(5) to convert directors into receivers for creditors would cause Section 3a(5) to be used to impair the obligation of the contract between the directors

and shareholders in violation of Article I, Section 10 of the U. S. Constitution and Article I, Section 16 of the California Constitution. The shareholders have never consented to have their elected Directors act as servants of creditors.

"(d) *Shareholders would be deprived of control of the Corporation without 'due process of law.'*

"To interpret Section 3a(5) to mean that the Directors of Crateo are converted into Trustees for creditors on filing of dissolution proceedings would deprive the shareholders of their control over the corporation and to that extent deny them of their property rights without 'due process of law' and violate the 14th Amendment to the U. S. Constitution.

"(e) *Violates law of common sense.*

"In addition to violating the Federal and State Constitutions, it violates the 'law of common sense' to interpret 3a(5) to change the meaning of the California Corporations Code to convert Directors into Trustees for Creditors.

"The shareholders and their representatives, the Directors, want to minimize or eliminate the creditors' claims; the creditors, on the contrary, want to maximize their claims. The Directors under California Corporations Code Section 4801 must 'defend suits brought against the

corporation.' To require the Directors to act in the best interests of creditors flouts every concept against 'conflict of interest' that is known in the law.

. . ."

(2)

The Requirement that the Trustee be "Disinterested" was Raised Below.

Crateo raised the point of the need for a disinterested Trustee in its Opening Brief to the Ninth Circuit, #73-3208, pages 8-12. It stated in that brief, in relevant part:

"As already discussed, under California corporate law, the directors remain directors of the corporation, they do not become trustees, and the application of *Bonnie* is, accordingly, improper.

"The Court in *Blair*, also furnishes guidance with respect to the definition of 'receiver' or 'trustee.' The court in *Blair* described a receiver as follows:

'A receiver is an indifferent person between the parties to a cause, appointed by the court to receive and preserve the property or fund in litigation pendente lite, when it does not seem reasonable to the court that either party should hold it. He is not the agent or representative of either party to the action, but is uniformly regarded as an officer of the court. . . .' 471 F.2d at 181.

"Crateo's directors do not fall within this definition. They continue to owe their duty to the corporation and retain the discretion to continue the corporation's business as they deem appropriate."

(References are to *In Re Bonnie Classics* 116 F.Supp. 646 (S.D.N.Y. 1953) and *Blair & Co., Inc. v. Foley* 471 F.2d 178 (1972).)

In Appellant's Opening Brief before the Ninth Circuit #74-2615, Crateo again pointed out the California requirement for a disinterested person:

"Under the laws of the State of California . . . California Code of Civil Procedure Section 565 provides that upon dissolution of any corporation the Superior Court may appoint one or more persons to be receivers or trustees of the corporation, but Section 566, immediately following thereafter, declares that:

'*No party* or attorney of a party, or a person interested in an action, or related to any judge of the court by any consanguinity or affinity within the third degree, can be appointed receiver therein without the written consent of the parties filed with the Clerk.'

(California Code of Civil Procedure Section 566)

In Appellant's Opening Brief to the Ninth Circuit #74-2615, a comparison of the attributes of Receiver/Trustee with that of Directors, was made. The following specifically deal with the requirement of disinterest:

"Receiver/Trustee	Directors
"Trustee elected by creditors. (The alleged *Bankrupt, its officers and directors may not vote.*) Receiver appointed by Court.	Elected by Shareholders. (Cal.Corporations Code 4803.)
Creditors nominate Receiver and Trustee. (The alleged *bankrupt, its officers and directors may not nominate.*)	Shareholders nominate the directors.
Prospective Receiver/ Trustee must be shown prior to appointment to be *free from allegiance adverse to general creditors.*	Directors have a definite bias in favor of shareholders.
Receiver hires attorney, normally with permission of Court. Attorney owes allegiance to creditors. Full disclosure of adverse interests of attorney required. *Attorney for Corporation is barred from employment.*	Directors hire their own attorney. Attorney owes allegiance to Corporation and its Shareholders. (Cal. Corporations Code 4801.)

Referee or Trustee is required to affirmatively furnish any information which indicates a bankruptcy offense has been committed.	Directors owe fiduciary duty to Shareholders not to improve the case for the creditors.
If a Receiver or Trustee has an interest adverse to the creditors it may be a bankruptcy crime.	Directors (who are often also shareholders) represent shareholders and have interest adverse to creditors. "

Appellant's Brief #74-2615. (Italics added) Pages 34-35.

(3)

Crateo Called the Court's Attention to the Fraud as soon as it Discovered it.

Petitioner (Appellants) Opening Brief to the Ninth Circuit in Case #74-2088 devoted 21 pages to the fraud and its discovery. It included photostatic copies of the forged signatures and the report of the Examiner of questioned documents which the Nevada Court had before it.

The Affidavit dealing with the discovery of the fraud was filed with the U. S. District Court, Southern District of California (Trial Court) on January 30, 1974, coupled with a motion to perpetuate testimony. This was only 12 days after "discovery" and included the Christmas holidays. The Affidavit stated in relevant part:

"On the 18th of December 1973, affiant had a telephone conversation with Mr. Jack Donnelly, Attorney at Law, 2655 Fourth Avenue, San Diego, California, Attorney Donnelly represented and now represents the Estate of Wilbur Clark, Deceased, and Toni Clark, the widow of Wilbur Clark. In the course of this conversation Attorney Donnelly informed your affiant that the note in the face amount of $780,000.00, bore the signature of a purported maker of that note, one Toni Clark, and that handwriting experts for both the bank (that is, the Southern National Bank of Houston) and Toni Clark agreed that the signature was a forgery. . ."

"That the information received from Attorney Jack Donnelly as hereinbefore set forth refers to that certain promissory note in a face amount of $780,000.00 executed by or guaranteed by Wilbur Clark and Toni Clark, Clayton Blakeway, Mrs. Clayton Blakeway, William Ward, III, and Mrs. William Ward, and secured by a second deed on a hotel in Austin, Texas. Toni Clark was a maker of that promissory note. That Referee Fox, acting as a Master in the within matter, in finding of fact No. 2 in the Fourth Report filed found that Crateo, Inc. had "debts" totaling $750,621.56. That the 'purported debt' of Southern National Bank of Houston constituted $293,647.61, or approximately 40% of this total debt."

In its Petition for Rehearing filed June 10, 1976, Crateo pointed out to the Ninth Circuit:

"5. THE COURT ERRS IN ASSUMING THAT THE APPELLANT COULD OR SHOULD HAVE DISCOVERED THE MATTER SOONER.

"The knowledge of the forgery was discovered after the trial, as was the decree establishing it.

"An affidavit of WALTER WENCKE, filed in the District Court, in connection with the post-judgment motions, and unrefuted, establishes the manner in which the information came to light. It came in a telephone call on December 18, 1973, after the trial. Since the charge here is concealment from the Courts of the judgment establishing the forgery, it is no answer to say the concealment was successful." (Petition for Rehearing, page 11) Nos. 73-3208, 74-2088, 74-2615, 75-3061.

(4)

The Right of the Court Below to Attack the Concealment Practiced Upon it was Briefed Below.

Petitioner, in its Reply Brief in Case #74-2615, filed January 16, 1975, in the Court below, asserted:

"1. <u>This Court has the Inherent Power to Exclude 'Rotten Fish' Claims</u>.

"Appellees argue in Point 1 of their response that the fraud tainted judgment by the Southern National Bank of Houston against Crateo is not subject to collateral attack in these proceedings. Instead they argue it should be set aside in Texas." (page 7)

"If the fraud of the Bank is patently evident and the nondisclosure of the fraud took place before this Court, why should this Court require a circuitous and time consuming procedure in Texas before it simply disregards the fraud?" (page 9)

"III. Appellees also do not discuss the fact that the concealment of the second judgment took place in the Court below.

"We point out, as we have in previous Briefs, that the fraud of concealment of the forgery after it was known, took place in San Diego, in the U. S. District Court. The Order of Judge Turrentine appointing Mr. Holzman as a Receiver (found as an exhibit in Appellants Opening Brief in 74-2615) recites in the preamble as among those present 'John M. Seitman of Seales, Patton, Ellsworth & Corbet (sic) for Southern National Bank of Houston'. The agents for the Bank, present in Court at the time of the Order, were silent when they should have spoken.

"The only thing that this Honorable Court is requested to do is recognize the fraud tainted judgment for what

it is - fraud; and deny to Appellees the benefits of that fraud.

"Let me give an example:

"A, B, & C put fish into a scale. D is to pay cash for those three fish. A's fish is rotten. We see the rottenness and smell the foulness of A's fish. The Bankruptcy Court determines that D is bankrupt because of the value of those three fish.

"Appellees, Intermark et al., are arguing the weight of those fish, including the rotten stinking fish, should be used to determine the dollar value of the creditors.

"We are simply arguing that this Court has a common sense duty to recognize the rotten fish *before* it, and that people don't pay for rotten, stinking fish. (page 9)

"SUMMING UP:

"1. Appellees are coming up with a theoretical legal position that someone must first go to Texas to get a Court Order in Texas setting aside a fraud which has already been demonstrated and adjudicated in Nevada.

"2. This argument ignores the quagmire of practical and legal problems that such a position would create (i.e. - who are the Receivers, who initiates, who controls, what is the source of funds, etc.)

"3. Appellees position is that they can avail themselves of the fruit of fraud until someone goes through the quagmire of these problems. They want "rotten fish" to be weighed in determining liabilities.

"4. When fraud is proved in Nevada, on a forgery not known to exist at the time of an earlier judgment in Texas, then this Court has the inherent right to disregard that earlier judgment and accept the second judgment in which the fraud was discovered as the 'res judicata' judgment.

"5. Further, when the 'nondisclosure' of the fraud takes place in the Court below, that 'act of silence,' when one should have spoken, is within the purview of this Court." (page 10)